UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

OSCAR PRIVATE EQUITY INVESTMENTS, Individually And On Behalf of All Others Similarly Situated, Plaintiffs, v. ROYCE J. HOLLAND and ANTHONY PARELLA, Defendants.	No. 3:03-CV-2761-K

APPENDIX TO PLAINTIFFS' SUPPLEMENTAL SUBMISSION REGARDING CLASS CERTIFICATION LOSS CAUSATION ISSUES ON REMAND FROM THE FIFTH CIRCUIT COURT OF APPEALS

VOLUMES I & II

-END VOLUME I-

DATED: November 1, 2007

Respectfully submitted,

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IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

OSCAR PRIVATE EQUITY INVESTMENTS, Individually and o/bo all others similarly Situated	:	
Plaintiffs	:	Civil No. 3:03-CV-2761-H
Royce J. Holland and Anthony Parella	:	
Defendants	:	

Second Report of Candace L. Preston, CFA in Support of
Plaintiff's Motion for Class Certification

Background, Qualifications and Assignment

1. I am a founding partner of Financial Markets Analysis, LLC and submit this report in support of Plaintiff's Motion for Class Certification. My qualifications have previously been set for in the Report of Candace L. Preston in Support of Plaintiff's Motion for Class Certification ("Preston Report") dated September 21, 2004 (Exhibit 1 to Appendix of Exhibits in Support of Plaintiff's Motion for Class Certification), filed with the Court on October 24, 2004). In addition, I submitted the Rebuttal Report of Candace L. Preston, CFA in Response to Holland and Parella's Opposition to Plaintiff's Motion for Class Certification (the "Preston Rebuttal Report") dated January 7, 2005.

2. The Preston Report dealt with the efficiency of Allegiance Telecom, Inc. ("Allegiance") common stock. In its opinion *Oscar Private Equity Investments vs Allegiance Telecom,* 487 F. 3rd 261, dated May 16, 2007, the Fifth Circuit held, consistent with my initial report, "that the market for defendant's shares has been demonstrated efficient by the usual indicia." Additionally, the Court indicated, "detail event studies supporting a finding that Allegiance's stock reacted to the 'entire bundle' of negative

information contained in the 4Q01 announcement," suggests market efficiency. The Preston Rebuttal Report addressed whether or not the corrective disclosure regarding the restatement of line count by Allegiance in its February 19, 2002 press release and analyst conference that followed caused a decline in the price of Allegiance common stock. However, as I was not tasked with providing more than a market efficiency analysis for class certification, I did not perform further analyses to quantify the portion of the decline caused by the restated line count. The Fifth Circuit, citing *Greenberg* held that in a case where multiple items of information are released together, plaintiffs must show, at class certification, that it is "more probable than not that it was this negative statement, and not other unrelated negative statements, that caused a significant amount of the decline."[1] Indicating that my "further analyses" is what is missing, the Fifth Circuit, citing *Unger*, required the submission of "some empirically-based showing that the corrective disclosure was more than just present at the scene."[2]

3. In response to the Fifth Circuit's opinion, which did not require a precise quantification of the damages at this juncture, I have applied standard econometric measures to quantify that portion of the February 20, 2002 decline in Allegiance's stock price that is attributable to the disclosure of the restatement of line count. Based on my additional analyses, it is my opinion that the restatement of line count was responsible for a significant portion of the stock price decline on that day.

Information Reviewed

4. In addition to the information cited in the Preston Report and the Preston Rebuttal Report, in preparation of this report, I have reviewed the following information:

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[1] *Greenberg*, 364 F.3rd at 666.
[2] *Unger*, 401 F. 3rd at 320-21. *Oscar,* 487 F. 3rd at 271.

a. Opinion on the Appeal from the United States District Court for the Northern District of Texas, filed May 16, 2007;

b. Transcript of the Allegiance Conference Call, February 19, 2002;

c. Transcripts from the deposition of Brett Messing;

d. Various deposition exhibits; and

e. Documents produced by certain securities analysts in conjunction with this litigation.

Loss Causation

5. The Fifth Circuit catalogs the information items released to the market after the close of trading on February 19, 2002, which may have contributed to the stock price decline on February 20, 2002 including:

a. A restatement of the total installed-line count from 1,140,000 to 1,015,000, a difference of 125,000;

b. A miss of analysts' expectations on 4Q01 and 2001 earnings per share;[3]

c. A greater EBITDA loss than some analysts expected; and

d. A very thin margin of error for meeting revenue covenants for 2002.[4]

6. It has long been accepted by economists and market participants that in order for information to have an effect on stock prices, it must be new – i.e. not simply a confirmation of information that has already been disseminated.[5] In the Preston Rebuttal Report, I briefly discussed the information that was disclosed on February 19, 2002, and concluded that the restatement of lines contributed to the stock price decline that occurred the following day. I have performed additional work to support my opinion that the

[3] To the extent that the full fiscal year loss was greater than expected, such a miss is encompassed in the fourth quarter results, since results for the nine months ended September 30, 2001 were already known.
[4] It was well known that Allegiance had escalating quarterly revenue covenants in 2001. The quarterly revenue covenants for 2001, as well as the full-year 2002 revenue covenants, were previously disclosed to investors by Allegiance as early as May, 2001.
[5] See, for example: Fama, E. F., Fisher, L., Jensen, M. C., & Roll, R., (1969). The Adjustment of Stock Prices to New Information. <u>International Economic Review, 10</u>(1). ; Brooks, R. M., Patel, A., & Su, T. (2003) How the Equity Market Responds to Unanticipated Events, <u>Journal of Business, 76</u>(1).

restatement of line count caused a portion of the $1.14 residual price decline in Allegiance stock on February 20, 2002.[6] I will address each potential negative item disclosed on February 19, 2002, including those set forth above.

7. I have categorized the information that entered the market on February 19, 2002, after the close of trading, and possibly caused Allegiance's stock price decline as follows: **Operational** (line additions and the restatement of line count), **Financial** (i.e. earnings and guidance related), and **Funding Status** (debt covenants and access to credit lines). It is my opinion that the **Operational** items caused a $0.91 reduction, with the restatement of lines accounting for $0.83 of that total; the **Financial** items caused an additional $0.05 reduction; and **Funding Status** combined with increased market uncertainty and the reduction in management credibility following the Q4 disclosures, accounted for the remaining price decline.

Operational

Allegiance Surprised the Market with a Line Count Restatement on February 19, 2002

8. Allegiance regularly reported certain operating metrics, including the number of installed lines ("line count") to the investment community. Line count was tracked internally by the Company and was forecasted by the Company. Those forecasts for installed lines were shared with the investment community, and the analysts following Allegiance at the time published estimates for the number of

[6] The "residual" price change is the expected price, using a regression equation which nets out the overall movement in the market in general, as well as a telecom sector index, minus the actual price change. Residuals are measured for significance using a t-statistic. T-statistics with an absolute value of 1.96 or greater demonstrate significance at the 95 percent level of confidence; T-statistics with an absolute value of 1.68 or greater demonstrate significance at the 90 percent level of confidence. The regression equation used here to measure the events of February 19 and 20, 2002 was developed using a control period of 4/24/01 – 2/19/02 and the Nasdaq Composite Index as well as an equal-weighted index of telecom CLEC (competitive local exchange carrier) companies as the independent variables. The regression equation is as follows: 0.00 + 1.36 * (Nasdaq index return) + 0.68 * (CLEC index return). The absolute price change on February 20, 2002 was negative $1.05 per share; the residual price change was negative $1.14 per share. A graph of Allegiance's stock price, the Nasdaq Composite index, and the CLEC index, on an equivalent basis, is attached as Exhibit E.

installed lines at the end of each quarter. For example, in connection with Allegiance's analyst conference in Dallas, Texas in May 2001, it forecasted "continued growth and expansion", including net line installs of 560,000 in fiscal year 2001, and revenues of $550 million. The presentation also included a chart that projected Allegiance's enterprise value ("EV") per line of $1,600, based on a stock price of $15.00 and estimated year end lines installed of 1,085,500.[7]

From Slide: (in millions) EV = $1,721 Local Access Lines Projected Year End 2001 = 1.085500 EV ÷ Line Count = 1,781/1.085500 = 1,585 (approx. 1,600)

EV is a common financial calculation used to value a company as a whole. For a public company such as Allegiance, EV is commonly defined as the market value of the equity plus the value of the debt minus cash. The market value of the equity of the company is calculated by multiplying the shares outstanding by the price per share.

9. Analysts following the Company during the proposed Class Period recognized the importance of line count in assessing the Company's future revenue growth. A number of the analysts who followed Allegiance calculated EV per line based on the estimated number of lines installed.

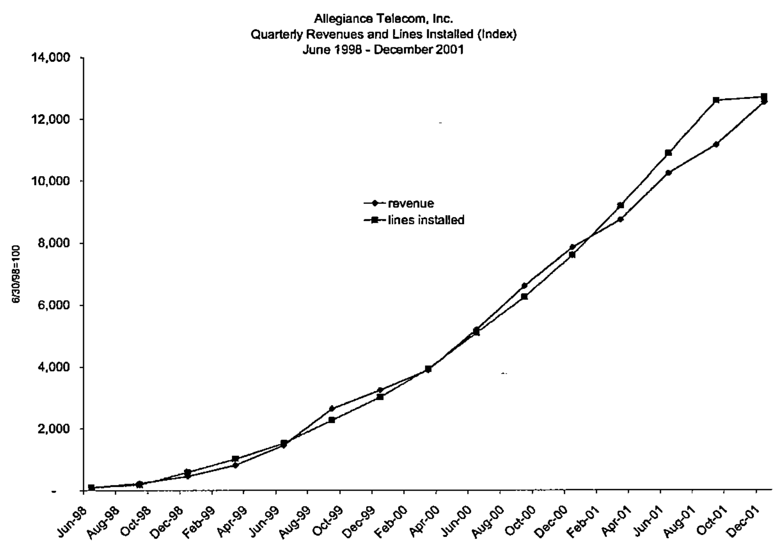
- *The company trades in line with the CLEC average when measured by FV/access line.*[8] *Such multiples vary according to perceived quality and growth and margin potential.* (JP Morgan H&Q: January 26, 2001)

- *Current enterprise value per 2001E ending lines of 1,169,700 is $709,*[9] *which is well below the benchmark acquisition price of $3,000 per access line seen in recent years.* (First Union Securities, Inc.: September 25, 2001)

[7] Algx-Fin 00134.
[8] FV is "firm value", which is synonymous with EV.
[9] A large component of EV is the stock price; changes in the stock price affect the EV/line count metric. The stock price declined from $15 in May to approximately $5.00 in September. This accounts for difference in EV/line count between May 2001 and September 2001.

• *On a per-line equivalent basis, we now project a Total Enterprise Value per line of about $2,000, compared with $2,500 in our previous valuations.* (Stephens Inc.: September 27, 2001)

10. Growth in line count was an important operating metric because there was a strong, positive relationship between line count and revenue. Revenue forecasts started with the number of installed lines which were then multiplied by the expected average revenue per line, sometimes described as "ARPU", or average revenue per unit.[10] The graph below, illustrates the historical correlation between Allegiance's installed lines and revenue:



11. On February 19, 2002, in addition to reporting financial performance for Q4 2001, Allegiance reported certain operating metrics including, for example, the addition of two new markets in Pittsburgh and West Palm Beach/Boca Raton; the completion of its fully-funded network buildout; and Q4 net lines installed of 135,000. In addition, Allegiance disclosed a restatement of previously reported line count, by 125,000 lines, as a result of an audit of its back-office systems. The restatement took the market by

[10] Allegiance calculated it by taking total revenue for the quarter and dividing it by the arithmetic mean of the quarter's beginning and ending line counts in Allegiance's order management system. The result is then divided by three (months in the quarter) to calculate average revenue per line.

surprise, as Allegiance was known for its superior back-office systems and previously unblemished record of delivering operating and financial results. The restatement was ill-received by the market.

12. Prior to the restatement, Allegiance touted its back-office systems which analysts perceived to be a competitive advantage.

> • *Allegiance realized from inception that strong back-office systems capable of scaling up as the company grew would be crucial to consistently and predictably provisioning unbundled loops. To this end, the company has invested heavily to create a world-class back-office system...Allegiance's back-office platform is a unique competitive advantage.* (JP Morgan H&Q: January 26, 2001)
>
> • *Importantly, the company has developed advanced operating support systems that provide for excellent visibility into its line additions and revenue. This provides us with comfort with our more conservative financial estimates...Allegiance boasts the industry's top back office systems, in our opinion.* (UBS Warburg: July 30, 2001)

The market was surprised by the restatement, and questioned the accuracy of the systems generating information regarding the most basic input to their projections – the line count.

> • *While an adjustment to reported lines is not uncommon in the industry, the magnitude of this restatement raises some concerns about the strength of the company's much trumpeted back office operations and how conservative, versus necessary, the company's bad debt reserves have been.* (Lehman Brothers: February 20, 2002)
>
> • *There were 135,000 net lines installed in 4Q '01, versus our estimate of 150,000 which brings total lines installed to 1,015,000. The company made a significant adjustment to its line count methodology, during 4Q '01...The company made a negative adjustment of about 125,000 lines.* (Salomon Smith Barney: February 19, 2002)
>
> • *On its conference call, the company said that it would continue ongoing database reconciliation, but it did not anticipate any more major corrections like this one.* (Goldman Sachs Global High Yield Research: February 20, 2002)
>
> • *Unfortunately, Bears will have additional fodder during 1Q02, as ALGX scrubbed their databases and found some differences in line count between billing and order management platforms. Consequently, management reduced the cumulative installed line base by approximately 126,000 lines to a new total of*

> *1,015,000...In light of "Enron-it is," we believe an increasingly skeptical market will have a negative view of this adjustment... Unfortunately, the line revision will cloud the company's otherwise strong performance.* (Hibernia Southcoast Capital: February 20, 2002)

13. In the days and weeks following the February 19, 2002 press release and conference call, the market continued to be concerned about the restatement of line count. On March 5, 2002, two weeks after the line count restatement, Allegiance management presented at the Credit Suisse First Boston ("CSFB") Global Telecom CEO Conference. CSFB published a report the following day underlining to the market's continued concern with the line count restatement.

> • *In an attempt to quell investor concerns, Holland once again reviewed the line reconciliation that occurred during 4Q01, given the announcement was a surprise to investors. As we noted in our report dated Feb 19 entitled 4Q Rpt'd: Qtr In Line but Local Trends Weak. Cutting ests; Maintain Hold, ALGX made a reconciliation to correct a discrepancy between its order management system and its billing system which accumulated over the last 4 years and resulted in a downward adjustment to lines in service of 125,000. We do not anticipate ALGX making further material adjustments to its line base in the future.* (CSFB: March 6, 2002)[11]

14. Using standard econometrics, adopted by the investment community in looking at telecommunications companies, I applied the market value multiple approach to estimate the stock price impact of the restatement in line count.[12] I calculated the EV/line count metric just prior to the restatement of line count. Doing this calculation allowed me to isolate that portion of the price decline that resulted from the restatement of lines. I first calculated Allegiance's enterprise value before the February 19, 2002 announcement. This calculation is based upon known balance sheet figures at the time from Q3 2001, disclosed in Allegiance's Form 10-Q filed November 14, 2001, including market value of equity of $424 million (114.56 million shares times $3.70 per share); debt of $983 million and cash of $538 million for a total EV of $869 million. I then divided the EV by

[11] The February 6, 2002 report appears to be misdated as it discusses events on "March 5, 2002".
[12] See, for example, Pratt, Shannon P., The Market Approach to Valuing Businesses, John Wiley & Sons, Inc., 2001, p. 4.

1,152,850 (the number of lines at the end of Q3, plus expected installs in Q4) to calculate the EV/line metric. My calculation resulted in a value of $754 per line before the announced restatement.

15. Substituting the restated number of lines for the erroneously reported lines, I was able to calculate the expected EV based on the restated number of lines (keeping all other variables constant). I calculated that the decline in EV due to the restatement of the lines was $95 million. Since neither the debt nor the cash changed, and I assumed Q4 installs came in as expected, this decline is entirely attributable to the line count restatement. Dividing $95 million by 114.56 million shares yields a change in equity value due to the restatement of the line count of $0.83 out of the total residual price decline of $1.14.[13]

Restated Line Count

(millions)		As of 2/19/02		As of 2/20/02
Stock Price		**$ 3.70**	**Value per Share @ EV/Installed Line = 754**	**$ 2.87**
Shares Out	x	114.56		114.56
Equity Market Value	=	423.85		328.90
Debt	+	983.21		983.21
Cash	-	537.58		537.58
EV	=	869.49	EV @ EV/Installed Line = 754	774.53
Q3 Installed Lines		1.00590	Q3 Installed Lines	1.00590
Expected Additions Q4	+	0.14695	Expected Additions Q4	0.14695
Line revision	-	-	Line revision	(0.12590)
Q4 Lines Installed*	=	1.15285	Q4 Lines Installed*	1.02695
EV/Installed Line	=	754	EV/Installed Line	754

Change in Equity Value/Share $ (0.83)

*Assumes Q4 additions as expected; isolates impact of restatement

16. Notwithstanding the restatement of lines installed, Allegiance also reported adding fewer lines during the quarter than expected, which would also have contributed to the decline in the price of Allegiance stock as a result of the February 19, 2002 announcement. I compiled the analysts' estimates of line additions for Q4 and attach a summary below.

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[13] A residual return of negative 13 percent, or -$0.48 per share, is the minimum threshold return that would be statistically significant at the 5 percent level given the regression equation described above.

Source: Published Research Reports

Date	Source	Line Adds
2/19/2002	Salomon SmithBarney	150,000
2/19/2002	CSFB	145,000
2/20/2002	Lehman	149,300
2/25/2002	KBRO	147,389
2/20/2002	Thomas Weisel	145,000
2/20/2002	RBC Capital	145,000
Average:		146,948

On average, the market expected Allegiance to add approximately 147,000 lines during the quarter. It added only 135,000 lines. Including the elimination of almost 126,000 lines due to the restatement, the net line additions were just 9,000. The shortfall in the lines added, in my opinion, also had a negative impact on the price of Allegiance's shares. I did not include the shortfall in line additions in calculating the negative impact on the stock price from the restatement of line count, but show those results below.

Includes Shortfall in Q4 line additions

(millions)		As of 2/19/02		As of 2/20/02
Stock Price		**$ 3.70**	**Value per Share @ EV/Installed Line = 754**	**$ 2.79**
Shares Out	x	114.56		114.56
Equity Market Value	=	423.85		319.89
Debt	+	983.21		983.21
Cash	-	537.58		537.58
EV	=	$ 869.49	EV @ EV/Installed Line = 754	$ 765.52
Q3 Installed Lines		1.00590	Q3 Installed Lines	1.00590
Expected Additions Q4	+	0.14695	Actual Additions Q4	0.13500
Line revision	-	-	Line revision	(0.12590)
Q4 Lines Installed	=	1.15285	Q4 Lines Installed	1.01500
EV/Installed Line	=	754	EV/Installed Line	754
Change in Equity Value/Share		**$ (0.91)**		

Financial

Allegiance Reported Q4 Earnings Below Analysts' Estimates

17. I have attached as Exhibit A a copy of the press release Allegiance issued at 5:01 pm on February 19, 2002, entitled: *Allegiance Telecom Announces Solid Fourth Quarter and Year-End Results With Annual Revenue Growth of Over 80 Percent.* The press release trumpeted that Q4 revenues grew 12 percent as compared to Q3; and annual

revenues increased by more than 80 percent. It included a projection of continued annual revenue growth for fiscal year 2002 of 50 percent, to $800 million. It also emphasized "significantly" improved operating margins and projected to be EBITDA positive in the second half of fiscal year 2002. The press release did not discuss the $1.09 per share loss for Q4, which was included in a table on the 7th of 14 pages of the press release, recognizing that revenue growth and EBITDA were the primary financial metrics of interest to investors at the time.

18. It is my opinion that only a negligible amount of the total stock price decline on February 20, 2002 was caused by Allegiance reporting Q4 net loss per share of $1.09, versus analysts' estimates for a loss of $0.97 per share for the following reasons:

a. Earnings per share ("EPS") and price-to-earnings ("P/E") multiples were not used to value start-up telecommunications companies at the time. Allegiance, along with most of its peers, was generating large losses as they built their networks and acquired customers. Analysts were primarily concerned with revenue growth, funding, and the ability to reach the targeted inflection point at which Allegiance would begin to generate positive cash flow (EBITDA).[14]

b. The Company did not provide EPS guidance, nor did the banks include a minimum EPS measure in its debt covenants.

c. The majority of analysts following Allegiance at the time reported that Q4 results were essentially in line with expectations (see below).

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[14] See for example, US Bancorp Piper Jaffray, 2/20/02 – "Note, we currently consider revenue, EBITDA, and capex the relevant metrics to track, as Allegiance is in the growth phase of its life cycle, in which cash flow and access to capital are most important."
Also, Damodaran, Aswath, Investment Valuation, John Wiley & Sons, Inc., 1996, p. 307.

d. The nature of the discrepancy between the reported Q4 EPS and analysts' expected Q4 EPS made the difference less significant. The $1.09 net loss included $5.5 million, or approximately $0.05 per share, of non-recurring charges related to prior acquisitions, the nature of which would not generally reflect a company's core earnings ability.

Allegiance Reported Q4 EBITDA loss of $22.2 Million

19. Allegiance's EBITDA loss for Q4 was $22.2 million (adjusted to exclude one-time charges) as compared to management's guidance for an EBITDA loss of $20 to $22 million.[15] The EBITDA loss for the quarter was largely in line with analysts' estimates and slightly below Company guidance. In fact, during the conference call, a transcript of which is attached as Exhibit B, Thomas Lord, Allegiance's CFO, described the Q4 EBITDA performance as being "in our target" of a loss of $20 - $22 million.

• *ALGX reported 4Q01 rev of $152Mn, slightly better than our $150Mn est. The company generated an EBITDA loss of $28Mn, in-line with our est of a loss of $21Mn when adjusting for a $5.5Mn non-recurring charge to SG&A – equating to a loss of $22Mn.* (Deutsche Bank Alex. Brown, February 20, 2002)

• *On 19 February, Allegiance Telecom (ALGX) reported fourth quarter earnings with revenue of $151.8m, up 12.4% sequentially (JPM estimate: 8.9%). Normalized EBITDA (excluding a $5.5m one-time charge associated with grooming its back-office systems) improved to a loss of $22.2m (JPM estimate: loss of $23.8m).* (J.P. Morgan: February 21, 2002)

• ***Allegiance Reported Results Inline With Expectations.*** *Allegiance Telecom reported 4Q01 revenue that was inline with the lower end of expectations while the remainder of the reported results were within guidance.* (Bear Stearns: February 19, 2002)

• *Results were in line with revised expectations with accelerating revenue growth and contracting EBITDA losses.* (Lehman Brothers: February 20, 2002)

• *On Feb 9, ALGX rpt'd 4Q01 results with total revs in line with our est. and with EBITDA, net of non-rec $5.5M chg, slightly ahead of our f'cst.* (Credit Suisse First Boston: February 19, 2002)

[15] Sources: UBS Warburg 2/20/02; Bear Stearns 11/12/01.

• *As expected, Allegiance reported weak revenues and in-line adjusted EBITA loss for Q4:01.* (Robertson Stephens: February 20, 2002)

20. In their original opposition brief, Defendants' erroneously describe the Q4 EBITDA loss as "worsening". EBITDA only "worsened" if one-time charges are included. In fact, as Allegiance touted, EBITDA was $4.2 million better than the EBITDA loss in Q3 of $26.4 million; and the EBITDA *loss* margin improved in Q4 to 14.6 percent from 19.6 percent in Q3. The Company emphasized the EBITDA loss of $22.2 million and the EBITDA margin improvement in its February 19, 2002 press release.

• *Margins also improved significantly with consolidated EBITDA loss of $22.2 million (excluding non-recurring charges associated with acquisitions).* (Allegiance press release: February 19, 2002)

21. Based on my review of the evidence as to Company guidance and market expectations for Q4 2001 EBITDA, and my professional experience, I believe that the reported Q4 EBITDA results had a minimal impact on the price of the stock on February 20, 2002.

<u>Allegiance Confirmed Revenue Guidance and Lowered EBITDA Guidance for Fiscal 2002</u>

22. The Company provided guidance in the February 19, 2002 press release and during the conference call with analysts for operating results for fiscal year 2002 including as follows:

a. The installation of 600,000 net new lines

b. Revenue growth in excess of 50 percent to $800 million

c. Continued margin improvement; turning EBITDA positive in the second half of 2002

d. Full year EBITDA loss of $15 to $25 million

23. Most of the guidance was confirmatory, and already reflected in analysts' estimates for the fiscal year. However, the EBITDA guidance reflected a reduction from management's prior guidance of negative $10 to $15 million. While the reduction in guidance overall for the year did not change the expectation for turning cash flow positive in the second half of 2002, it did cause analysts to reduce their EBITDA estimates overall for the year.

24. In addition, while the revenue guidance of $800 million was nominally confirmatory, Allegiance had made an acquisition in the prior month which some analysts expected might add to fiscal year 2002 revenues. Thus, the confirmation was perceived by some to reflect a softening in the revenue outlook. In addition to forward EBITDA estimate revisions, analysts also lowered their estimates for fiscal year 2002 revenue.

- *On the revenue front, Allegiance reiterated prior revenue guidance of $800 million for this year. The prior expectation was issued before the carrier's acquisition, late in the fourth quarter, of Intermedia Business Internet, a Tier-1 backbone provider that had been owned by WorldCom. IBI's continuing revenue contribution to Allegiance is difficult to estimate at this point, but we expect that it will be material enough for us to interpret the carrier's non-adjustment of revenue expectations to represent a decline in expectations for the underlying business relative to a few months ago.* (Stephens Inc.: February 20, 2002)

25. In general, the market and stock prices are said to be "forward looking" in that the stock price reflects the present value of future cash streams associated with owning the security.[16] To that extent, investors are concerned with a company's future earnings prospects, which manifest in the estimates formulated and published by analysts. Generally speaking, corporate and general economic events that cause a negative change in analysts' forward revenue and/or earnings expectations result in the diminution of

[16] See, for example: Brealey, Richard A., and Myers, Stewart C., Principles of Corporate Finance, (7E) McGraw Hill, 2003, Ch. 7 – The Value of Common Stocks. Also, Sharpe, William F., Alexander, Gordon J., and Bailey, Jeffery V., Investments, (6E), Prentice Hall, 1999, Ch. 17 – The Valuation of Common Stocks.

stock prices. I believe that management's reduced EBITDA guidance, and a perceived weakened outlook for revenue growth, was partially responsible for the stock price decline that occurred on February 20, 2002.

26. Telecom sector analysts discussed certain valuation metrics in formulating investment recommendations and "target" prices for the stocks, including EV/revenue and EV/EBITDA multiples. In the case of Allegiance, the EV/EBITDA multiple was not meaningful because Allegiance, as with many other telecoms, was in a growth phase, not generating positive EBITDA, and not expected to generate positive annual EBITDA for some time. EV/revenue was a relevant financial metric used to value Allegiance as well as other telecoms.

27. I calculated the average change in analysts' fiscal year 2002 revenue and EBITDA estimates, immediately following the February 19 press release and earnings conference call (see Exhibit C). On average, there was a $5 million reduction in estimated revenue and a $4 million reduction in EBITDA attributed to the event in question.[17] Based on Allegiance's closing stock price of $3.70 per share on February 19, 2002, I calculated the EV/revenue multiple, based on the unrevised revenue estimates to be 1.1. I applied the average reduction in analysts' revenue estimates for fiscal year 2002 by the revenue multiple and arrived a change in equity value of negative $5.7 million, or $0.05 per share.

[17] I averaged the revenue and EBITDA forecasts before and after the February 19 press release and conference call, and calculated the average change in each.

Reduction in 2002E Revenue

(millions)		As of 2/19/02		As of 2/20/02
Stock Price		**$ 3.70**	**Value per Share @ EV/Revenue 1.1**	**$ 3.65**
Shares Out	x	114.56		114.56
Equity Market Value	=	423.85		418.17
Debt	+	983.21		983.21
Cash	-	537.58		537.58
EV	=	869.49	EV @ EV/Installed Line = 1.1	863.80
2002E Revenue		792.61	Revised 2002E Revenue	787.42
EV/Revenue	=	1.1	EV/Installed Line	1.1
Change in Equity Value/Share	**$**	**(0.05)**		

28. As mentioned, since EBITDA was projected to be negative, any EV/EBITDA multiple calculation would be meaningless. However, I noted that the reduction in revenue estimates was larger than the reduction in the EBITDA estimates, and since the revenue change would flow through to the EBITDA line, the effect on the stock price from the reduction in EBITDA estimates would be subsumed in and not additive to the $0.05 reduction I calculated.

Funding Status

Allegiance Disclosed Quarterly Minimum Revenue Requirements Under Bank Facility Covenants

29. During the earnings conference call, management affirmed the Company was in compliance with all aspects of its debt covenants related to its bank credit facility. Allegiance's CFO, Mr. Lord, assured the investment community that they "did not see any covenant risk," that the Company had adequately covered the 2001 revenue requirement of $445 million (recording 2001 revenue of $516.9 million), and that management was forecasting that they would exceed both the quarterly and annual minimum revenue tests for 2002. In addition, Royce Holland stated, "We will be in comfortable shape just like we were in 2001 on making those covenants." The Company had previously disclosed minimum quarterly revenue requirements for fiscal year 2001,

as well as the full-year 2002 requirement.[18] The only new "news" was the breakdown, by quarter, for the 2002 requirement. There was no change revealed on February 19, 2002 regarding the overall covenant or guidance. For example, one month earlier, the analyst from J.P. Morgan commented:

- *Finally, we believe the incremental revenue generated from the acquisition will add cushion to the company's ability to meet its $755 million revenue covenant for 2002 against guidance of $800 million for the year.* (J.P. Morgan: January 4, 2002)

30. Allegiance took the opportunity to disclose the minimum quarterly revenue covenants at this time because there was considerable uncertainty in the market regarding the funding status of telecom companies, as several of Allegiance's competitors had violated, or were close to violating, certain debt covenants, and several were on the verge of bankruptcy.[19] Given my review of the news articles, the conference call transcript, and analyst reports that directly addressed Allegiance's debt covenants and funding status, it is my opinion that the market largely adopted management's optimistic view that it would meet the minimum quarterly revenue covenants laid out for fiscal year 2002, and that it was well funded to achieve its business plan.

31. Further, my analysis demonstrates that it was not until Allegiance reported financial results for Q1 2002, *two months after* the end of the proposed Class Period, that the market's opinion regarding the safety of those covenants began to change. Thus, in my opinion, the February 19 disclosure of the quarterly revenue covenants alongside the Company's guidance for revenue; and management's pledge that Allegiance would not violate those covenants allowing it full access to the remaining line of credit, did not cause any meaningful decline in the price of Allegiance's stock on February 20, 2002.

[18] See for example, Clay Myers deposition pp. 51-54.
[19] For example, McLeodUSA and Global Crossing, Ltd. filed Chapter 11 bankruptcy in January, 2002.

• ***Management tackles covenant concerns.*** *In light of investor's negative sentiment concerning CLEC funding woes, management took time during the call to explicitly address its bank covenants. Specifically, the Company indicated that it has had no problems meeting its covenants and our estimates (see below) also point to the same conclusion.* (McDonald Investments: February 20, 2002)

• *We are persuaded that Allegiance will likely continue to have adequate protection against normal business risk as it proceeds toward the point when it can begin generating cash. On yesterday's conference call, Company management showed that Allegiance has cleared loan covenant hurdles relating to revenues, EBITDA, indebtedness and capital spending with relative ease, and appears to be in position to do the same in 2002.* (Stephens Inc.: February 20, 2002)

• *On the conference call, the company stated that it is currently in compliance with all of its debt covenants. There is some risk to the 2002 revenue covenant of $755 million (2002 quarterly revenue covenants: $155 million in Q1:02; $180 million in Q2:02; $200 million in Q3:02; and $220 million in Q4:02). However, we believe that the covenant could be amended, if necessary, especially given that any miss in the numbers would be slight.* (Robertson Stephens: February 20, 2002)

• *Given that the company remains fully funded, in our estimation, and within its debt covenants, we believe the outlook remains solid.* (BB&T Capital Markets: February 20; 2002)

• *We believe both the minimum revenue covenants and at least the low-end of guidance are achievable. The new guidance however does not take into account the impact of the recently acquired Intermedia Business Internet assets, the revenue contribution for 2002 from this business will be unknown until probably mid-year...* (Deutsche Banc Alex. Brown: February 20, 2002)

• ***Debt covenants only a minor issue.*** *Our estimates provide sufficient breathing room for the Company to remain compliant with its debt covenants.* (US Bancorp Piper Jaffray: February 20, 2002)

32. While there were a few analysts who expressed concern that the "cushion" between their projections and the covenants was slight, overall they adopted management's view that the covenants were surmountable and that Allegiance was fully funded in 2002.[20] <u>Allegiance, in fact, never violated its minimum revenue requirements</u>.

[20] Only the analyst from Lehman Brothers forecasted a slight covenant violation in Q402, adding, "However, the recent acquisition of Intermedia operations may provide some upside to these projections and close the potential shortfall."

The minimum revenue requirements, and actual reported revenue for the first three quarters of 2002 were as follows:

	1Q 02	2Q 02	3Q 02
Minimum revenue	155	180	200
Guidance	165-168	180-190	208-213
Actual	162.1	184.4	219.5

In July, 2002, five months after the end of the proposed Class Period, Allegiance announced it was in discussions with its lenders to amend its debt covenants to align more closely with its transition to profitability.[21] In November, 2002, more than nine months after the end of the Class period, it announced its lenders granted it a waiver from its existing covenants, including the minimum revenue requirements, until April 2003.

33. Allegiance's minimum revenue requirement for Q4 01 was $140 million. It actually earned $152 million, demonstrating 60 percent growth over the prior year's fourth quarter. Its full year 2001 revenue requirement was $445 million. Allegiance earned $517 million, an 80 percent increase over the prior year. These results, which were reported on February 19, 2002, demonstrated that even in a turbulent market, Allegiance was generating strong revenue growth and was on track to achieve its forward revenue guidance.

34. As further support for my opinion that the disclosure of the revenue covenants caused no real change in the outlook for Allegiance, or its stock price, Fitch Ratings, Ltd., an international credit rating agency, made no changes to Allegiance's debt rating upon obtaining the minimum revenue requirements. Allegiance provided the quarterly covenants to Fitch one month prior to their public release on February 19, 2002. On February 20, 2002, Fitch affirmed its B+ rating on Allegiance's senior secured debt. Fitch's comments are as follows:

[21] See Allegiance press release, dated July 30, 2002, attached as Exhibit F.

> • *A major factor that led to the bankruptcy filings and recapitalizations of many of ALGX's competitors was their inability to meet bank covenants. To date, ALGX has not been in danger of violating any of its covenants. Its most stringent covenant in 2002 is its quarterly revenue covenant, requiring $755 million in revenue for 2002 ($155 million 1Q '02; $180 million 2Q '02; $200 million 3Q '02; $220 million 4Q '02). The current public forecast is $800 million, and Fitch believes if demand for IAD remains strong and the company is able to continue to successfully provision the service, it will satisfy its revenue covenant...By Fitch estimates, the current business model is fully funded.* (Fitch Ratings: February 20, 2002)

35. It wasn't until two months <u>after</u> the end of the proposed Class Period, that meeting the revenue covenants became an issue. On April 30, 2002, after the close of trading, Allegiance reported Q1 2002 revenues of $162 million, which met the minimum revenue requirement of $155 million, but fell short of management's guidance. Immediately following the shortfall, some analysts downgraded the stock, citing the covenants, which resulted in a significant decline in the stock price. On May 1, 2002, Allegiance's stock price suffered a negative 24 percent residual decline, from $2.03 to $1.52 per share. It continued to decline over the next several days. Analysts made the following comments regarding the revenue shortfall:

> • *Revenue short of expectations...Downgrading to a Hold given proximity to covenants amid difficult environment. This was a tough quarter for Allegiance, and the outlook remains uncertain. To meet its revenue covenants for full-year 2002, the company has to increase its revenue 46% over 2001, or approximately 10% sequentially. For the remainder of the year...We think this may prove difficult given the current economic and regulatory environment. Revenue covenants are becoming a larger concern for the company, which we have listed below. ...given the company's proximity to its bank facility revenue covenants amid the difficult telecom and overall economic environment, we are lowering our rating to a Hold (3).* (BB&T: May 1, 2002)

> • *We feel it will be difficult for ALGX to meet its 2Q02 revenue covenant of $180Mn, which would require adding $18Mn in incremental revenue after adding only $10Mn in 1Q02 over 4Q01.* (Deutsche Bank Securities: May 1, 2002)

Previously, after the Q4 2001 results were announced, the analyst from BB&T had concluded as follows:

• *Given that the company remains fully funded, in our estimation, and within its debt covenants, we believe the outlook remains solid. Long-term buy.* (BB&T: February 20, 2002)

36. Later, on June 18, 2002, Allegiance announced it made an acquisition that was likely to add $15M to revenue in the second half of fiscal year 2002. This acquisition largely alleviated concerns about the minimum revenue requirements for the remainder of the year. Allegiance's stock price increased by a statistically significant amount immediately following the announcement of this acquisition. The residual price increases on June 19, 20, and 21 were 23%, 17% and 23%, respectively. A chart showing the May 1, 2002 price decline, attributed to the revenue shortfall and concerns about covenant violations, and the subsequent increase on June 19, 20, and 21, as those concerns were largely alleviated due to the acquisition, is attached as Exhibit D. The same analyst from BB&T published the following comments regarding the acquisition:

• *The incremental revenue contribution from the service business will, it appears, be included. In the recent past, we had expressed concern over the company's ability to meet the revenue hurdle set forth within such covenants. It would appear at this time, without having spoken yet with management, that the addition of this revenue would allow the company to comfortably meet/exceed such covenants going forward.* (BB&T: June 18, 2002)

37. Thus, given the evidence I have examined, it is my opinion that the February 19, 2002 disclosure of the quarterly minimum revenue requirements for fiscal year 2002 did not contribute meaningfully to the stock price decline on February 20, 2002.

Additional Factors Considered

38. In the months following the September 11, 2001 terrorist attacks, business conditions for telecom companies deteriorated, and lenders were reluctant to fund telecom operations. As a result, many telecoms sought bankruptcy protection or reorganized, eliminating shareholder value in the process. Further, in late 2001, energy trader Enron filed for bankruptcy and its auditor Arthur Andersen (also Allegiance's

auditor) was under SEC investigation for delinquent accounting. It was into this turbulent market that Allegiance announced, among other things, a restatement of previously reported line count.[22] It is my belief that the restatement itself created some amount of distrust in the reported numbers, and diminished management credibility, and contributed to the stock price decline on February 20, 2002.

• *While results were about as expected and pretty good considering the economic environment, the company's call was not without its issues. The reconciliation of lines between databases was unexpected, and while it probably does mean some lower level of expense in 2002, and doesn't really impact 2002's revenue ramp (ARPU was artificially low as a result in the nine months prior), it also raises questions.* (Thomas Weisel Partners: February 20, 2002)

• *While we commend management for wiping the slate clean before entering 2002, the magnitude of this adjustment (12% of total) makes it difficult to swallow. Prior to this, the quality and transparency of management's reporting has been second to none, in our opinion. This is the first time in our recollection that one can question management's reporting. Given the issues surrounding accounting today, the timing of such an adjustment could not have been worse.* (BB&T Capital Markets: February 20, 2002)

39. Quantifying the effect of diminished credibility is difficult. I have not currently added it to the price impact I calculated as a direct result of the line count reduction, although arguably the effect on shareholder losses was substantial.

40. In conclusion, my further analyses lead me to conclude that it is "more probable than not" that the restatement of line count contributed significantly to the $1.14 residual stock price decline on February 20, 2002. I have preliminarily estimated that, on a line count equivalent basis, $0.83 of the residual decline can be attributed to the reduction in Q401 line count. I understand that discovery is ongoing. My opinions are based upon documents and data provided to or obtained by me to date, and are subject to revision

[22] During Allegiance's conference call on February 19, 2002, Holland discussed, at length, the precarious market conditions in light of accounting scandals and telecom sector bankruptcies.

based on information that may later become available to me during the course of this litigation.

I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct. Executed this 31st day of October, 2007 at Princeton, New Jersey.

Candace L. Preston, CFA

Appendix:

I. Analyst Reports

II. Event Chronology

EXHIBIT A

PRN Allegiance Telecom Announces Solid Fourth Quarter and Year-End
Feb 19 2002 17:01

Results With
Annual Revenue Growth of Over 80 Percent

-- 4Q01 Revenues of $151.8 Million - Increased by 12.3 Percent Compared With 3Q01 and 59.8 Percent Compared with 4Q00
-- 2001 Revenue of $516.9 Million, 81.2 Percent Increase Compared With 2000
-- Pittsburgh and West Palm Beach/Boca Raton Service Initiated -- Allegiance Telecom's 35th and 36th Markets -- Planned Build-out Now Complete
-- 16 Markets Pre-Overhead EBITDA Positive in 4Q01, Driving Overall Company EBITDA Loss Margin from 31.5 Percent in 4Q00 to 14.6 Percent (excluding non-recurring charges of $5.5 million) in 4Q01
-- 17 New Collocations for a Total of 789, Addressing Approximately 20.43 Million Business Lines "On-Switch"
-- Acquisition of IBI Tier 1 Internet Backbone from WorldCom

DALLAS, Feb. 19 /PRNewswire-FirstCall/ -- Allegiance Telecom, Inc. (Nasdaq: ALGX), an integrated communications provider (ICP), today announced results for its fourth quarter and year-end 2001. Allegiance reported fourth quarter revenues of $151.8 million, an increase of 12.3 percent compared with 3Q01 and full year 2001 revenues of $516.9 million, an annual growth rate of over 80 percent. Margins also improved significantly with consolidated EBITDA loss of $22.2 million (excluding non-recurring charges associated with acquisitions).

"The year 2001 was a challenge for most businesses both in terms of a slumping global economy and specifically for the telecom industry which has endured a massive shakeout of weaker or poorly capitalized companies. Despite these environmental challenges, Allegiance Telecom continued to post solid results throughout the year as evidenced by our top line growth of more than 80 percent while significantly improving margins," said Royce J. Holland, chairman and CEO of Allegiance Telecom. "With the activation of our 36th and last market in December 2001, Allegiance is now at an operational inflection point where our focus is shifting from the rapid deployment of networks to a rapid path to profitability. We continue to forecast revenue growth in excess of 50 percent in 2002 while at the same time improving margins with a goal of turning EBITDA positive during the second half of this year. This strong continuing growth is in stark contrast to the low single digit growth rates of our major competitors, the incumbent local exchange carriers (ILECs) and major interexchange carriers," he said. "At the close of 2001, Allegiance reached a long-awaited milestone. With our 36-market network buildout complete, we are the one company poised to address more than half the business lines in the United States," Holland said.

"And, as the one company with the largest network footprint serving the SME sector today, Allegiance has reinforced its competitive position as the leading nationwide competitor to the regionally focused incumbent carriers," Holland said.

Holland further stated that the Company is forecasting the following financial and operational targets in 2002:

-- Installation of approximately 600,000 net new lines with Integrated Access and other T1 delivered voice and data services constituting the largest number of new installs.
-- Revenue growth in excess of 50 percent, resulting in a 2002 revenue target of approximately $800 million. This is unchanged from the previous forecast.
-- Continued margin improvements with a goal of turning EBITDA positive in the second half of 2002. This is unchanged from the previous forecast.
-- Activation of SONET fiber networks to replace leased capacity in 2 new markets resulting in a total of 24 markets with fiber networks. Addition of 61 new collocations for a total of approximately 850 by year end.
-- A capital expenditure (capex) budget in the range of $215 million to $240 million with most of the capex being driven by new installs on a success basis, and most of the remainder driven by fiber and collocation deployment. This is a change from the previous capex forecast of $225 million to $250 million.

"Despite the economic recession and continuing shakeout that have continued into the first quarter, we are forecasting another high growth year in 2002 and are looking forward to achieving the milestone of turning EBITDA positive," added Holland. "We believe that a 2002 performance at or near our forecasted targets will clearly establish that profitable high growth enterprises can thrive even in a poor economic climate."

Network Rollout Continues On Schedule

With the addition of two new markets, Pittsburgh in November and West Palm Beach/Boca Raton, Fla. in December, Allegiance Telecom completed its fully-funded network buildout. Today, 36 U.S. markets are operational including: Atlanta, Austin, Baltimore, Boston, Chicago, Cleveland, Dallas, Denver, Detroit, Fort Lauderdale, Fort Worth, Houston, Long Island, Los Angeles, Miami, Minneapolis/St. Paul, New York, Northern New Jersey, Oakland, Ontario/Riverside CA, Orange County, Philadelphia, Phoenix, Pittsburgh, Portland, Sacramento, St. Louis, San Antonio, San Diego, San Francisco, San Jose, Seattle, Tampa, Washington D.C., West Palm Beach/Boca Raton and White Plains, NY.

Allegiance Telecom continued to post strong gains in its addressable market during 4Q01, adding 17 new collocations. At the end of December, the Company was collocated in 789 central offices for unbundled loops, representing an addressable "on-switch" market of approximately 20.43 million local business access lines.

Allegiance has 31 telecommunications switches in operation, supporting the following markets: Atlanta, Austin, Baltimore, Boston, Chicago, Cleveland, Dallas & Fort Worth (2), Denver, Detroit, Houston, Los Angeles, Miami & Ft.

Lauderdale & West Palm Beach/Boca Raton, Minneapolis/St. Paul, New York & Long Island & White Plains (2), Northern New Jersey, Orange County & Ontario/Riverside, Pittsburgh, Philadelphia, Phoenix, Portland, Sacramento, St. Louis, San Antonio, San Diego, San Francisco & Oakland, San Jose, Seattle, Tampa and Washington, D.C.

Network Improvement: Metro Rings and Long Haul Fiber

During 4Q01, Allegiance continued upgrading its network with the lighting of metropolitan fiber rings. To date, 22 Allegiance markets (Austin, Boston Chicago, Dallas, Denver, Detroit, Ft. Worth, Houston, Long Island, Los Angeles, New York, Northern New Jersey, Philadelphia, Phoenix, Pittsburgh, Portland, St. Louis, San Antonio, San Diego, Seattle, Washington, D.C. and White Plains) are now served by fiber. These rings provide improved network capacity, operational efficiency, improved financial margins and route redundancy, further increasing the reliability of the Allegiance network. Long haul fiber rings now connect Allegiance switch sites in Boston, New York, Philadelphia and Washington D.C.

Financial and Operational Highlights

Allegiance Telecom posted a strong sales increase for the quarter, with lines sold increasing from 182,000 lines in 3Q01 to 190,000 in 4Q01, an increase of 4.4 percent compared with 3Q01 and an increase of 25 percent compared with 4Q00.

Net lines installed during the quarter were approximately 135,000, essentially flat with the net lines installed in 3Q01. The 4Q01 net line installations reflect the negative impact of the Sept. 11 tragedy that significantly affected sales in September and thereby reduced the backlog of orders entering the quarter. In addition, the Company took an adjustment to its installed base of lines as a result of the data reconciliation project discussed below.

For the fourth quarter and for the year ended December 31, 2001, Allegiance Telecom had consolidated revenues of $151.8 million and $516.9 million, respectively. This represents an increase of 12.3 percent as compared with 3Q01 and an annual increase of 81.2 percent over 2000. Allegiance continued to use its capital to support the development of new markets, resulting in a fourth quarter EBITDA (earnings before interest, taxes, depreciation and amortization, excluding management ownership allocation charge and non-cash deferred compensation expenses) loss of $27.7 million ($22.2 million before non-recurring charges of $5.5 million associated with acquisitions) and capital expenditures of $45.4 million. The Company continued on its path to profitability with EBITDA loss as a percent of revenue for the quarter at 14.6 percent (excluding non-recurring charges of $5.5 million) versus 19.6 percent in 3Q01 and 31.5 percent for 4Q00. For the full year 2001, Allegiance posted an EBITDA loss of $106.7 million (excluding non-recurring charges associated with acquisitions) and capital expenditures of $364.4 million.

Gross margin continues to be strong; for 4Q01, Allegiance Telecom's gross

margin was 51.3 percent, consistent with 3Q01 gross margin of 51.4 percent and up from 50.4 percent in 4Q00.

"Allegiance Telecom used approximately $95.9 million of its cash and short-term investments during the fourth quarter to fund its operations, capital expenditures and service its indebtedness. This represents a reduction of $20.2 million from the $116.1 million used to fund operations, capital expenditures and service indebtedness in the 3Q01. The remainder of our cash used in 4Q01 was for acquisitions and investments in working capital. Net cash interest payments were $19.2 million in 4Q01 and $24 million for the full year 2001," said Thomas M. Lord, Allegiance executive vice president of corporate development and chief financial officer. "At December 31, 2001, Allegiance had an undrawn committed credit facility of $150 million and approximately $400 million of cash and short-term investments."

Back Office System and Process Upgrades

In the fourth quarter, Allegiance made significant progress in its continuing program to automate manual processes and develop electronic system interfaces to monitor work queues and improve process visibility and database consistency and integrity. A major milestone was the implementation of the Singl.eView by ADC billing system for one of the new cities, Pittsburgh, and for new customers in Philadelphia. In 2002, Singl.eView will be implemented for new customers on a market by market deployment schedule through the end of the third quarter 2002.

In 2Q01, the first automated billing interface (BIF) was implemented for unbundled loop customers between the provisioning systems and the legacy billing system -- the Abiliti platform. The elimination of manual keying of billing information into Abiliti produced two benefits. First, it eliminated the lag time (which sometimes had been over two months) in producing a new customer's first bill -- and even more important, on a going forward basis it virtually eliminated data entry errors caused by manual keying into the billing system. In the fourth quarter 2001, the automated billing interface was implemented for the Singl.eView platform for unbundled loop customers.

In 4Q01, work also began on the development of automated billing interfaces to eliminate the manual keying of data into the billing systems for Integrated Access and other T1-based products, and MACD (moves, adds, changes and disconnects) orders. These interfaces between provisioning and both the Abiliti and Singl.eView platforms for T1 delivered products, and for disconnects, are currently in testing with implementation scheduled for completion by the end of the first quarter 2002. The manual keying of new installation and disconnect information into billing will then be eliminated.

Coincident with the deployment of Singl.eView and the development of automated billing interfaces, the Company has been conducting a database reconciliation project to reconcile the order management, provisioning and billing databases for inconsistencies that had developed in the past. These inconsistencies are related to a number of factors, including as a result of manual data entry into these systems. The reconciliation project resulted in the identification and correction of discrepancies in line count between the

databases.

As a result of the reconciliation, the line count in the order management system, which is the basis for tracking line count, has been adjusted downward approximately by 125,000 lines to conform with the line count in Allegiance's billing systems. The adjustment includes 95,000 facilities lines and 30,000 resale lines and results in a starting point for 2002 of 1,015,000 lines in service of which 93 percent are facilities based. The inconsistencies between the various databases had an immaterial ($5 million or less) impact on revenue because most of the adjustments are to the line count in the order management and provisioning system, not the billing systems. ARPU (average revenue per unit) for Q401, however, increases to $50.08 per line as a result of the reconciliation project.(1)

Another very significant back office system upgrade is scheduled for completion by the end of February 2002. After several months of Beta testing, Allegiance Telecom will have its trouble ticket systems fully bonded with SBC. During the 2001 testing period, Allegiance was able to enhance the customer care experience and expedite repair activity by providing customers with real time trouble ticket updates as a result of information exchanged between Allegiance and SBC through a new electronic interface. With trouble ticket bonding completed, the process of "telephone tag" between Allegiance and SBC is replaced by a real time, interactive exchange of information to expedite the resolution of trouble tickets. As previously with electronic bonding for provisioning of new orders, Allegiance plans to use the system interfaces developed in cooperation with SBC to expedite trouble ticket resolution with the other ILECs.

Tier 1 Internet Backbone Acquired

At the end of 4Q01, Allegiance acquired substantially all of the Intermedia Business Internet (IBI) assets from WorldCom, Inc. Terms of the deal were not disclosed but Allegiance confirmed that the transaction purchase price was not financially material. WorldCom was obligated to sell the IBI assets pursuant to a consent decree entered into by WorldCom and Intermedia with U.S. Department of Justice in connection with their merger last year.

"The acquisition of a true Tier I Internet backbone that has peering status with all major providers, including a three-year peering agreement with UUNET, will decrease our costs of terminating Internet traffic," said Dan Yost, president and COO of Allegiance Telecom. "We believe the Tier I backbone represents a great opportunity to further expand our data offerings and leverage our existing customer base of small and medium sized businesses that already rely on Allegiance Telecom for local voice service."

Regulatory Certifications

Allegiance Telecom is certificated to provide local exchange services in 24 states and Washington D.C., including Arizona, California, Colorado, Florida, Georgia, Illinois, Indiana, Minnesota, New Jersey, New York, Maryland, Massachusetts, Michigan, Missouri, Nevada, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, Texas, Virginia, Washington State and

Wisconsin.

Corporate Background

Based in Dallas, Allegiance Telecom is a facilities-based integrated communications provider (ICP) offering businesses a complete package of telecommunications services, including local, long distance, international calling, high-speed data transmission and Internet services. Allegiance is currently operational in 36 U.S. markets. The Company's Web address is: www.algx.com . Allegiance's common stock is traded on the Nasdaq National Market under the symbol ALGX.

Certain statements in this press release constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, and the Company intends that such forward- looking statements be subject to the safe harbors created thereby. The words "believes," "expects," "estimates," "anticipates," "plans," "will be" and "forecasts" and similar words or expressions identify forward-looking statements made by or on behalf of the Company. These forward-looking statements were derived using numerous assumptions and are subject to many uncertainties and factors that may cause the actual results of the Company to be materially different from those stated in such forward-looking statements. Examples of such uncertainties and factors include, but are not limited to, the Company's ability to timely and effectively provision new customers; the Company's ability to retain existing customers; the Company's ability to obtain additional financing should it be necessary to do so; the Company's ability to develop and maintain efficient billing, customer service and information systems; and technological, regulatory or other developments in the industry and general economy that might adversely affect the Company. Additional factors are set forth in the Company's SEC reports, including but not limited to the Quarterly Report on Form 10-Q for the quarter ended September 30, 2001. The Company does not undertake any obligation to update or revise any forward-looking statement made by it or on its behalf, whether as a result of new information, future events or otherwise.

(1) Average revenue per line is calculated by taking total revenue for the quarter and dividing it by the arithmetic mean of the quarter's beginning and ending line counts in Allegiance's order management system. This result is then divided by three (the number of months in the quarter) to calculate average revenue per line.

ALLEGIANCE TELECOM, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except share and per share amounts)

Three Months Ended	Three Months Ended	Year Ended	Year Ended

	December 31, 2001 (unaudited)	December 31, 2000 (unaudited)	December 31, 2001	December 31, 2000
Revenues	$151,818	$95,029	$516,888	$285,227
Network Costs	73,991	47,173	251,734	150,718
Gross Margin %	51.3%	50.4%	51.3%	47.2%
Selling, General and Administrative	105,508	77,780	377,386	252,368
Depreciation, Amortization and Noncash Compensation	75,703	51,653	260,986	147,433
Loss From Operations	(103,384)	(81,577)	(373,218)	(265,292)
Other Income (Expense)				
Interest Income	927	11,943	15,664	56,969
Interest Expense	(23,142)	(16,601)	(74,259)	(69,244)
Other Income (Expense), net	(22,215)	(4,658)	(58,595)	(12,275)
Net Loss Applicable to Common Stock	$(125,599)	$(86,235)	$(431,813)	$(277,567)
Net Loss Per Share, basic and diluted (A)	$(1.09)	$(0.79)	$(3.82)	$(2.58)
Weighted Average Shares Outstanding, basic and diluted (A)	114,835,954	109,636,885	113,115,871	107,773,112
Other Financial Data:				
EBITDA (B)	$(27,681)	$(29,924)	$(112,232)	$(117,859)
Capital Expenditures	45,407	98,115	364,396	430,817

Notes:
(A) The basic and diluted net loss per share reflect the three-for-two stock split, which occurred on February 28, 2000.
(B) EBITDA excludes non-cash compensation expense.

ALLEGIANCE TELECOM, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

	December 31, 2001	December 31, 2000
ASSETS		
CURRENT ASSETS:		
Cash, cash equivalents, and short-term investments (A)	$399,316	$670,911
Other current assets	167,090	99,366
Total current assets	566,406	770,277
PROPERTY AND EQUIPMENT		
Property and equipment	1,366,710	907,182
Accumulated Depreciation	(350,460)	(162,279)
Total property and equipment, net	1,016,250	744,903
NON-CURRENT ASSETS (B)	192,187	153,659
TOTAL ASSETS	$1,774,843	$1,668,839
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES	$139,474	$139,070
LONG-TERM DEBT	1,002,590	566,312
OTHER LONG-TERM LIABILITIES	24,703	4,972
STOCKHOLDERS' EQUITY	608,076	958,485
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$1,774,843	$1,668,839
COMMON SHARES OUTSTANDING	115,214,859	110,064,619

Notes:
(A) Includes restricted short-term investments of $0 and $12,952 at December 31, 2001 and 2000, respectively.
(B) Includes restricted long-term investments of $954 and $829 at December 31, 2001 and 2000, respectively.

Selected Operational Statistics

	As of December 31,	As of September 30,	As of June 30,	As of March 31,

	2001	2001	2001	2001
Markets Served	New York	New York	New York	New York
	Dallas	Dallas	Dallas	Dallas
	Atlanta	Atlanta	Atlanta	Atlanta
	Fort Worth	Fort Worth	Fort Worth	Fort Worth
	Los Angeles	Los Angeles	Los Angeles	Los Angeles
	Chicago	Chicago	Chicago	Chicago
	Boston	Boston	Boston	Boston
	Oakland	Oakland	Oakland	Oakland
	San Francisco	San Francisco	San Francisco	San Francisco
	Philadelphia	Philadelphia	Philadelphia	Philadelphia
	Washington, D.C.	Washington, D.C.	Washington, D.C.	Washington, D.C.
	San Jose	San Jose	San Jose	San Jose
	Orange County	Orange County	Orange County	Orange County
	Houston	Houston	Houston	Houston
	No. New Jersey	No. New Jersey	No. New Jersey	No. New Jersey
	Long Island	Long Island	Long Island	Long Island
	San Diego	San Diego	San Diego	San Diego
	Detroit	Detroit	Detroit	Detroit
	Baltimore	Baltimore	Baltimore	Baltimore
	Denver	Denver	Denver	Denver
	St. Louis	St. Louis	St. Louis	St. Louis
	Cleveland	Cleveland	Cleveland	Cleveland
	Seattle	Seattle	Seattle	Seattle
	Miami	Miami	Miami	Miami
	Minneapolis/ St. Paul	Minneapolis/ St. Paul	Minneapolis/ St. Paul	Minneapolis/ St. Paul
	Phoenix	Phoenix	Phoenix	Phoenix
	Tampa	Tampa	Tampa	Tampa
	San Antonio	San Antonio	San Antonio	San Antonio
	Ft. Lauderdale	Ft. Lauderdale	Ft. Lauderdale	Ft. Lauderdale
	Austin	Austin	Austin	
	Sacramento	Sacramento	Sacramento	
	Portland	Portland	Portland	
	White Plains	White Plains		
	Ontario/ Riverside	Ontario/ Riverside		
	Pittsburgh			
	West Palm Beach/ Boca Raton			

# of Markets	36	34	32	29
# of Switches	31	30	30	27
Central Offices Colocated	789	772	740	687
Addressable Markets (Lines) via Colocated Co's	20,430,000	19,850,000	19,090,000	17,810,000
Sales Headcount	1,584	1,571	1,612	1,471
Total Headcount	4,140	3,948	3,874	3,834
Lines Installed	1,015,000	1,005,900	869,700	733,900

*Note: Sales Headcount includes Sales Team Managers, Account Executives and Sales Administrators

ALLEGIANCE TELECOM, INC.
PERFORMANCE METRICS

	Actual 1999			
	1Q	2Q	3Q	4Q
Gross Margin %	24.0%	28.2%	43.0%	39.2%
SG&A as % of Rev	276.0%	173.4%	125.5%	107.4%
EBITDA as % of Rev	-252.0%	-145.2%	-82.6%	-68.2%
Annualized ($ in 000's)				
Average Revenue per Employee	$51.4	$65.8	$92.8	$95.0
SG&A per Employee	141.8	114.2	116.5	102.0
EBITDA per Employee	(129.5)	(95.6)	(76.6)	(64.8)
EBITDA per Line	(1.7)	(1.0)	(0.6)	(0.5)
Cum. Capital Expenditures per Line	3.1	2.7	2.2	1.9
Monthly:				
Average Revenue per Line	$51.76	$58.01	$70.46	$61.92
Network Expense per Line	39.34	41.63	40.17	37.66
SG&A per Line	142.86	100.62	88.46	66.49

PRN Allegiance Telecom Announces Solid Fourth Quarter and Year-End
Feb 19 2002 17:01

	Actual 2000 1Q	2Q	3Q	4Q
Gross Margin %	42.5%	45.2%	47.7%	50.4%
SG&A as % of Rev	101.8%	90.0%	87.2%	81.8%
EBITDA as % of Rev	-59.2%	-44.9%	-39.6%	-31.5%
Annualized ($ in 000's)				
Average Revenue per Employee	$98.7	$109.9	$116.7	$122.9
SG&A per Employee	100.5	98.9	101.9	100.6
EBITDA per Employee	(58.5)	(49.3)	(46.2)	(38.7)
EBITDA per Line	(0.4)	(0.3)	(0.3)	(0.2)
Cum. Capital Expenditures per Line	1.8	1.6	1.6	1.5
Monthly:				
Average Revenue per Line	$56.55	$58.17	$58.79	$57.21
Network Expense per Line	32.49	31.90	30.76	28.40
SG&A per Line	57.55	52.35	51.30	46.82

	Actual 2001 1Q	2Q	3Q	4Q
Gross Margin %	51.6%	51.0%	51.4%	51.3%
SG&A as % of Rev	79.9%	73.7%	70.9%	69.5%
EBITDA as % of Rev	-28.3%	-22.7%	-19.6%	-18.2%
Annualized ($ in 000's)				
Average Revenue per Employee	$119.6	$128.8	$138.2	$150.2
SG&A per Employee	95.6	94.9	98.0	104.4
EBITDA per Employee	(33.9)	(29.2)	(27.0)	(27.4)
EBITDA per Line	(0.2)	(0.1)	(0.1)	(0.1)
Cum. Capital Expenditures per Line	1.4	1.3	1.2	1.3
Monthly:				
Average Revenue per Line	$52.61	$51.58	$48.03	$50.08
Network Expense per Line	25.46	25.28	23.36	24.41
SG&A per Line	42.05	37.99	34.07	34.81

ALLEGIANCE TELECOM, INC.
MARKET FINANCIAL DATA

(Dollars in thousands)
(Unaudited)

FIRST 9 MARKETS (A)

	Actual 1999 1Q	2Q	3Q	4Q
LINES IN SERVICE	70,939	100,118	138,148	182,151
REVENUE				
Local Service	$15,927	$19,812	$23,999	$28,162
Long Distance	423	567	724	856
Data	393	674	1,843	2,696
Total Revenue	$16,743	$21,054	$26,565	$31,715
GROSS MARGIN %	39.5%	40.7%	49.5%	52.7%
PRE-OVERHEAD EBITDA (B)	($5,045)	($4,875)	($2,385)	$475
PRE-OVERHEAD EBITDA %	-30.1%	-23.2%	-9.0%	1.5%
ADDRESSABLE SWITCHED ACCESS LINES (C)	4,561,531	5,370,951	5,923,239	6,468,292
PENETRATION %	1.6%	1.9%	2.3%	2.8%

FIRST 9 MARKETS (A)

	Actual 2000 1Q	2Q	3Q	4Q
LINES IN SERVICE	228,208	274,740	316,592	376,046
REVENUE				
Local Service	$34,951	$39,142	$43,155	$46,088
Long Distance	1,287	1,582	2,144	2,553
Data	4,956	6,446	7,963	10,413
Total Revenue	$41,193	$47,169	$53,261	$59,054
GROSS MARGIN %	55.4%	54.7%	56.3%	57.1%
PRE-OVERHEAD EBITDA (B)	$4,922	$6,738	$9,103	$11,599

PRE-OVERHEAD EBITDA %	11.9%	14.3%	17.1%	19.6%
ADDRESSABLE SWITCHED ACCESS LINES (C)	6,990,236	7,556,349	7,887,217	8,051,487
PENETRATION %	3.3%	3.6%	4.0%	4.7%

FIRST 9 MARKETS (A)

	Actual 2001 1Q	2Q	3Q	4Q
LINES IN SERVICE	425,380	482,661	528,587	538,112
REVENUE				
Local Service	$48,752	$49,238	$51,396	$45,071
Long Distance	2,879	2,970	3,021	3,418
Data	12,537	14,161	16,801	24,209
Total Revenue	$64,168	$66,369	$71,218	$72,697
GROSS MARGIN %	59.0%	60.7%	61.3%	61.5%
PRE-OVERHEAD EBITDA (B)	$14,323	$17,345	$20,061	$20,239
PRE-OVERHEAD EBITDA %	22.3%	26.1%	28.2%	27.8%
ADDRESSABLE SWITCHED ACCESS LINES (C)	8,383,468	8,754,124	8,955,369	9,063,265
PENETRATION %	5.1%	5.5%	5.9%	5.9%

Notes:

(A) Includes New York, Dallas, Ft. Worth, Atlanta, Los Angeles, San Francisco, Chicago, Houston, and Boston.
(B) Represents earnings before interest, taxes, depreciation and amortization before corporate overhead allocation.
(C) Includes only lines on-switch.

SOURCE Allegiance Telecom, Inc.

-0- 02/19/2002

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/Web site: http://www.algx.com /

(ALGX)

CO: Allegiance Telecom, Inc.
ST: Texas
IN: TLS
SU: ERN

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EXHIBIT B

Allegiance Telecom Inc (ALGX) - Q4 2001 Earnings Conference Call

Allegiance Telecom Inc (ALGX) Q4 2001 Earnings Conference Call	Tuesday, February 19, 2002 5:00 pm

Fair Disclosure Financial Network, Inc. For more information: www.fdfn.com

THE OPERATOR:
Good day and welcome to the Allegiance Telecom fourth quarter release conference call. As a reminder today's conference is being recorded. (indiscernible) and introductions I will turn the conference over to Mr. Thomas Lord, Allegiance Telecom's Chief Financial Officer and Executive Vice President of Corporate Development.

MR. THOMAS LORD:
Before we begin I want everybody to know we've just contacted the various news services and our e-mail sources and I apologize. I think there is a slew of numbers that went out today but we have been told that your e-mail boxes should be receiving this if you not already received them, the Yahoo wires, the business wires, the PR wires, all of the stuff should be there eminently within seconds or minutes, and we do humbly apologize for the snafus in terms of the BackOffice process as it relates to getting out press releases. Before I begin I got to obviously go through and start with the traditional warning that on this call we will be making many forward-looking observations and statements. Royce is going to go into detail in terms of our guidance for 2002 and the support around that. In particular, we will be making forward-looking statements that are covered under the Safe Harbor Private Securities Reform Act and are subject to many uncertainties and risks. We have continued to disclose in our Qs and Ks and our earnings statements what these risks are and we urge everyone to continue to monitor those as well as these calls. We try our best to provide you all with as much of an update on the Company as possible. I'm only going to make about one minute's worth of editorial comments because I know no one wants to hear that. They want to get right into the facts. I think these editorial comments are very important. We've read the same papers that you all have read, we've seen the same TV shows and news articles that you all have seen, and on behalf of the Allegiance management team and Board of Directors that I will remind you are the largest owners of the Company, we understand our roles as stewards of the business, as caretakers of your investment and we gravely respect our role of accountability to all investors and to maintain as much

disclosure and insight into the business as possible. I've really have gone out of my way personally and shared the belief of the management team that we want to strive to try to have the highest standards possible for you all to have an insight into the business, no matter your opionion in terms of the business , be it positive or negative. I know that the sentiment out there's the worst I've ever seen in 25 years. I was visited by a leading investment bank last week, that kind of sums it up in terms of why there has been such pain and inability to separate good companies from bad. This bank provided me with a piece of paper that showed the bankruptcies in the telecom industry that went back from July 2000 through year-to-date and was rather staggering. The number of names were household names of a year or two ago and it is our objective and we hope after this conference call we will have provided you with some insight that we at Allegiance do not intend to try to get onto that list, get close to that list or have anything to do that list. We think we have a well managed, well funded, adequately capitalized business that will continue to grow in spite of the difficult economic environments, in spite of problems and the environment we are currently operating in, relative to our peers, there's no such thing as being in first place, but I think that Royce will tell you that we believe we've at least tied up there for the top. So, enough of my personal statements. Let me get right into the facts and figures and I'm going to do this as Walter Condit said, "just the facts, just the news, all the black and white. Fior the quarter, revenues came in at $151.8 million, that's up 12.3 percent sequentially, from 135 million. For the year, results were 518 million, up 81 percent from 285 million a year ago. A little bit of upside surprise, at least in terms of what we've said on the last call, gross margins came in at 51.3 percent, compared to 51.4 percent. I had expected those gross margins to have ticked down a little bit more but we had good network expense management throughout the quarter. For the year, gross margins improved 400 basis points, rising from 47.2 percent last year to 51.2 percent this year. SG&A came in at $105.5 million with a one-time non-recurring charge of $5.5 million, associated with duplications of some of our past acquisitions and endeavor to try to go clean the house as much as we possibly could. This increase from 95.9 million to 101.5 million was a 10 percent increase. For the year, SG&A increased by 48 percent, from 252.4 million last year to 373.3 million this year. The EBITDA loss for the quarter came in at 27.7 million. That would include, again, the 5.5 million non-recurring charge, so we believe we are in our target of trying to get the 20 to 22 million area, obviously on the highside. This compares with a $26.4 million loss, so on our organic basis, EBITDA dropped from 26 down to the 22 level. For 2001, the EBITDA lost dropped from 117.9 down to 108.6. We believe you will see continued improvements in our declining EBITDA losses throughout 2002 and we're reaffirming our guidance to go EBITDA positive in the second half of the year. The loss per share for the quarter came in at $1.09, this would compare with 94 cents sequentially int the third quarter and a loss for the year came in at $3.77 comparing with $2.58 last year. Our shares outstanding at the end of the year,

were 113 million with shares outstanding for the quarter came in at 114.8. Capital expenditures, and I'll touch on this when I talk about cash and liquidity in the big picture. CapEx dropped dramatically down to the 45.4 million for the fourth quarter, down from 88 million in the previous third-quarter. For 2001, capital expenditures dropped from 430 million in 2000 down to 364 million for this year. Liquidity, the number one topic on people's minds today. We remain in a very fortunate an enviable position. We closed the year with $400 million and 150 million of availability of a (indiscernible) that we've not yet tapped in terms of that excess liquidity that exists. So Today we have cash liquidity of $550 million. We are in compliance with all aspects of our covenants as it relates to 2001 and in terms of the budgets that we have passed on to our banks for 2002. We do not see any covenant risk. I promised all of you that on this we would give you detailed covenants for 2002 and I intend to do that now, as well as to provide some perspective with how we've fared against those covenants in 2001. The toughest covenant for us to go up against has been the revenue text. Let me give you some detailed numbers looking backwards before we look forward. In 2001 as you all know, our revenues went like this on a subsequent basis: 105 million in the first quarter, 124 million in the second quarter, 135 million in the third-quarter and 152 million in the fourth quarter are results for the year of 516 million. Our covenant test was 85 million in Q1, 100 in Q2, 120 in Q3 and 140 in Q4 with a covenant test of 445 million. So, we more than adequately covered that revenue test. The capital expenditures covenant test for 2000 was 400 million and we came in very comfortably at 364. For 2002, our clearly covenants on revenues in the first quarter are 155 million, increasing to 180 in the second quarter, rising to 200 in the third-quarter, and topping out at 220 in the fourth quarter, for total revenue covenants test of 755 million. Our capital expenditures basket is 400 million. There's not not a chance in Hell that we will spend $400 million. Two other items that we get asked about are our senior secured debt to total capitalization. At the end of this year, our $350 million draw down on the debt facility when added to approximately $65 million in (indiscernible) releases left us with a total senior secured debt number of $416 million, against total capitalization of approximately 2.8 billion. That ratio comes out at .15. Our covenants test is .35. Unless Allegiance was to go issue an immense amount, which we have no plans to, of additional debt, we are more than two times covered with respect to our senior secured debt to capitalization covenant test. The other debt capitalization test is total debt. That would include our high yield bonds. If you add the high yield bonds to our Senior Secured indebtedness you come up with about a total of around $1 billion of indebtedness against the capitalization of 2.8 billion. That ratio, when divided, produces a statistic of .36. Our covenants test is .6. As you can see, for good reasons, if I was a bank I would do the same thing. The banks have made sure that they have put themselves in a position where Allegiance will not over leverage itself. We have every intent to stay inside of those covenants with respect to the utilization of leverage. With the high yield market being closed, I don't think I got a chance in

Hell of taking the debt of this company up for this coming year. Back to the operational side. We've had a project underway this year, everybody knows about that's very important in terms of realizing improved gross margins. We exceeded our plan oin terms of the number of fiber rings that we had lit and operational. At the end of the second quarter we had 11 rings lit. It jumped to 14 in the third-quarter. We told people we thought we would ass 7 in Q4 and we ended up adding eight. Those new markets are Detroit, Phoenix, Pittsburgh, San Antonio, San Diego, Boston, Los Angeles and Long Island. We intend to add two to perhaphs three fiber rings for 2002. The other project that was completed in the fourth quarter still had some network grooming to go, but it has been lit and has been activated as our long haul fiber with MetraMedia (phonetic) fiber and level three providing us with long haul connections and call it one great big giant fiber ring in what Royce refers to as the bosh-wash corridor, well we now have connected (indiscernible) with Boston, New York, Philadelphia and DC that are in turn are linked into our fiber rings. Access, I know an issue we always get asked about but frankly, this question has kind of seen begun to go by the wayside. I don't get many questions about it but we will continue to report the statistic. The access trends continue to be favorable in terms of access declining as a percent of revenues, but I said in the past, I believe they have traughed off. In the first quarter, again to refresh everyone's statistical data base, access as a percent of gross revenues was 20.1 percent. It dropped to 14.9 percent in the second quarter. In the third-quarter it came in 12.6 percent and dropped to 12.2 percent for the fourth quarter. For the year, total access as a percent of revenues came in at 14.5 percent. In terms of the belief of our business plan, that it is scalable, demonstrable and has a path to profitability, in the first quarter we had 11 markets that were generating EBITDA positive results. In the second quoted that increased by two cities to 13. In the third-quarter we added one city up to 14. We're pleased to report that in this quarter and at the end of the year we added two cities to the roster of being cash flow positive, Denver and the New Jersey market, and now have a total of 16 markets that are generating positive EBITDA contributions to

the company's consolidated cash flows. Capital expenditures:
like I said, we're probably not going to be helping the equipment companies out as much as we have in the past years in our growth phase, but CapEx has dropped rather dramatically and will continue to decline. Capital expenditures for the year came in at 364 million, and the CapEx trend for the year went 121 million in the first quarter, 114 million in the second quarter, 88 million in the third-quarter and a dramatic drop off to 45 million in the fourth quarter. We are also lowering our CapEx guidance to by about ten million dollars this year, now down to a range of 215 to $240 million. A lot of that had to do with the fact that we had as a result of the IBI acquisition, our intent to purchase Cisco routers and things to try to grow our (indiscernible) backbone. By virtue of buying that asset, we did not have to spend moneyies that we were planning on spending in

terms of IP capital acquisitions. Coming back to the CapEx number for the year ago, though, to give people a sense that it is almost entirely growth driven, of 215 to $240 million, at the margin today, it cost us approximately $250-300 to add a line. Given that our target for this year is around 600,000 lines. you can see that as a result of growth, growth that we believe is a good thing, our total success based capital will come in at a range of between 152 to 180 million. The remaining $60 million in capital expenditures will be comprised of continued ongoing OSS upgrades and modifications as well as traditional maintenance capital expenditures to support our gold-plated network. Our RPU (phonetic) for the quarter improved, and Royce will touch on this when he goes into his component of the conference call, but RPU (phonetic) to remind everyone throughout the year, in the first quarter was $52.60, declined at $51.86 when the access rate declines took effect, with the impact in the third quarter as a result of the events of 9/11, and still suffering somewhat in the fourth quarter, we're pleased to report the (indiscernible) from $48.03 to $50.08. In terms of what drove the results for the quarter, let me give the breakdown now in terms of local, data and long distance. For the fourth quarter, our local voice revenues came in and 87.5 million, up 2.4 percent from 85.4 million and up 32.9 percent from 65.8 million a year ago. Out data business remains growing quite robustly as a result of the success we're having in the integrated access Services offering. Our data revenues increased 29.8 percent, rising from 41.9 million to 54.4 million for the fourth quarter. This was a 116 percent improvement over the results of 25.1 million dollars a year ago. I think if anybody in this call was to go back and try to refresh their memory a year ago, I think clearly, in spite of what we've read about with the data environment being somewhat weak, the damand we see from the SME sector really is quite robust is the leading driver why Tony has had success in the integrated access services offering. Our long distance business increased by 26.9 percent, rising from 7.8 million to 9.9 million, this was an increase of 141 percent from 4.1 million a year ago. And in summary, again, the quarter was 12.3 percent sequentially, from 135 million to 158 million for the fourth quarter and up 59.8 percent year-over-year, rising from 95 million a year ago. The breakdowns on the percentages, for the fourth quarter, local business came in at 57.7 percent, data came in at 35.8 percent and long distance came in at 6.5 percent. If you compare the trends to a year ago you've seen that data has been the drive in the Company's business. Our local voice a year ago was 69.2 percent, data was 26.4 percent and long distance was 4.4 percent. Now, some information in terms of statistics on the network and how the performed. We estimated installs in the fourth quarter of approximately flat with a third quarter of around 135,000. Tony's order book remained strong, coming in at 190,000 lines for the quarter, up 4.4 percent. We added two markets and have now completed the building stage of the network and are in the harvesting mode of trying to generate cash flows off of these 36 markets. We added one switch and now have 31 switches in operation. We added 17 lit (indiscernible) for total of 789. There are 21 colocations that were completed

during the year that were part of the CapEx and the cash burn but are not reported in my lit statistics since we have not deployed facilities to them. This is one of the reasons why we have a strong belief that the CapEx is going to continue to trend down. We added net 13 people to sales. Tony added two or three new sales teams during the quarter but we did make some changes to the sales organization and add some attrition and reductions in sales so that the overall sales organization has basically been held flat. The total Company headcount increased by 192 bodies with approximately 300 bodies coming on board at year-end from the IBI acquisition. That would tell you that on an organic basis outside of IBI we actually had a headcount decline at Allegiance by probably about 100 to 150 bodies. We expect that at the end of 2002, we will end up with approximately 850 colocations which would represent what we would believe would be our target market for addressing the large SME enterprise that we're targeting today. Accounts receivable and day sales outstanding. Again, we had improvement here in the quarter, albeit modest. Again, to review, in the first this year, our day sales outstanding stood at 94.5 days. It improved to 90.8 days in the second quarter. It dropped to 84.6 days in the third-quarter, and we're pleased to report that at the end of the fourth quarter our sales outstanding were 83.8 days. To put this in perspective, however, 25.2 days of the 83.8 days are comprised of receivables that take time to get paid from AT&T, Verizon, FPC, Ameritech and BellSouth. These leading corporations of high credit standing do pay their bills with us but it has always been a lagging type of a payment plan for them, I guess, and due to the disputes that go back and forth, the reason why we have 25.2 days, perhaphs you all can (indiscernible) them as to why they take so long to pay humble allegiance what they rightfully owe us. That would tell you that our day sales outstanding for our retail customer base which is what the organization is all about is 58.6 days, a rather respectable number. Now, in terms of what I said earlier about trying to find everything we could possibly find to exit the year and go into 2002 with robust outlook, we, Allegiance, not an audit committee not our auditing firm, not anyone else, we undertook our own witch hunt on our own books to try to come up with as much things as we could possibly find that could either be obselete, duplicated, whatever in an endeavor to try to create the best reserves and the fairest conservative representation of the Company's P&L and balance sheet going into 2002. We continued that trend in terms of taking the appropriate actions that are necessary, though we not experienced any changes in terms of payment patterns or seeing any part of the economy impact (indiscernible) over our client base (indiscernible) material level. Having said that, we did take higher than normal expenses in the quarter to continue to beef up our reserves. Our gross accounts receivable outstanding for the fourth quarter at the end of the year so you all will not have to wait for the 10K, was 184.1 million. Our net accounts receivable number is 141.4 million. We have total reserves of revenue reserves and bad debt reserves of $42.7 million, or 23 percent of my gross ER. In the quarter we added $11.5 million to our bad debt

reserves and made the addition of 5.5 million and onetime non-recurring charge or added a total of 16.6 million dollars to the reserve basis. I think one of the more conservative positions that is out there. I do have to come back, which I think is very important because cash is king, and show you all what the cash SG&A burn is inside the Company. This is what counts going forward and is the reason why we've had a dramatic improvement in terms of cash utilization. Our gross sgns trends for the year went like this, this would include the bad debt reserves and all other noncash items: in the first quarter gross SG&A was 77.8 million. It increased to 91.4 million in the second quarter. It increased to modestly to 95.9 million in the third quarter and rose to 105.5 million in the fourth quarter. The cash component to the SG&A was 73.3 million in the first quarter, 83.8 million in the second quarter, 83.1 million in the third-quarter, and 88.9 million in the fourth quarter. You can clearly see that our SG&A increases have dropped dramatically in terms of the rate of increased relative to previous periods and are now trending at almost a flatline environment, in fact of the fact that revenues continue to show significant sequential increases in the double digits and dramatic increases in terms of year-over-year trends. The (indiscernible) system had great improvement in the third-quarter and it's detailed in the press release. We mnow have all of the Broadband division, the city of Pittsburgh and new customers in Philadelphia happened turned life and we will complete the transition to move to an in-house billing system by the end of the third-quarter. The final thing I'm going to talk about before turning over to Tony, who will give you some insight in terms of what is going at AID, is the acquisition we made of the intermediate business assets from WorldCom. We are under a (indiscernible) nondisclosure, so I cannot get into the purchase price. There has been a lot of speculation as to what we paid for the asset. I think some of that speculation is fairly accurate but again, we cannot get into the details behind that. The principal drivers behind acquisition, however, have been very sanguine and explicit with people on this, as a function of the fact that we wanted to get a tier one backbone. Everybody knows we'ver been trying to do this for quite some time. Fortunately for us, we missed paying three or four hundred million for a tier one backbone a couple of years ago. At the heyday of the market there were many companies that were acquiring tier one backbones for the billion of dollars. So we think in this case being the turtle and the last one to cross the finish line was a good place to be in terms of our ability to have have now a pier agreement with (indiscernible) net, a world-class tier one backbone that we think will improve the customer experience, and most importantly, from my perspective, we'll save in network expense and we'll have an additive feature or an (indiscernible) feature with respect to gross margins going forward. The other question I've been asked is, what will this do to revenues in 2002? The answer that I've been giving people will be the same answer for at least the next one or two quarters, until we get our arms around the customer base, it will be a number that is not 0. It's obvious that it's going to add revenue, folks. We're going to prune off the whole sale business quite

quickly, however, Chris Maronowski (phonetic), who has headed up this operation, is working closely in an integration basis with the people that we're proud welcome at Allegiance and we're going to be reviewing on an account by account basis, which of those customers we should keep and which of those customers should turn away due to their being off net. Therefore, we commit to you during the first quarter of 2002 and the second quarter of 2002 to provide you with updates as to we think will be the installed established base from IBI that we will continue to own and keep moving forward. With that, I'm going to turn it over to Tony, who is going to walk you through and give you an update on what's happening in his world.

MR. ANTHONY PARELLA:
Welcome. I want to give you some ideas of what's changed in terms of the Broadband factory. We made and implemented many significant changes to the factory that,-I will share with you some pretty staggering results for January. First of all, we went from most of last year using outside contractors to install the vina boxes that we use that really are the brains behind the IAD platform. We now over the fourth quarter got all of our field operations people trained and we now today are putting in all of own vina boxes ourselves and pretty much done away with the use of contractors for extending the demarker and installing the boxes, which gives us much tighter control on the customer experience and installing the services as well as allowes us to keep score on a closer basis of the many we can process per day. No. 2, we made a number of significant software changes in the BackOffice that has allowed us to scale the IAD and total communication platform to the same level that we have the (indiscernible) platform and the third significant change that we did, we've consolidated a portion of the cut over process where local number portability is required. That means where our customer had existing phone numbers that they want to use on their integrated service. In the path that was decentralized by market. Over the fourth quarter we've consolidated that to Dallas and that one function, now the people who did it for (indiscernible) also do it for IAD, which is really allowing us some expanded efficiencies. To give you some color what it means to us as a Company, let me put to you this way: in the month of January, just the uni factory and the I-A D factory installed a record 60,000 lines. And here's the mix, for the first time, I installed as many I-A D customers or TC customers or dedicated Internet customers all under the heading of Broadband which you can see the significant of our data growth, and 50 percent of of the lines being unbundled loops. Fourth quarter came in with what I believe was a very strong quarter for sales and we've set up very well as you can see by the installs in January. But one of the things I don't think we've done a good enough job goods as the Company is explaining to our investors from a sales and marketing standpoint what makes Allegiance different. Why are we able to continue to sell and install number of lines needed to make our numbers when so many others have struggled? I'm going to try to drive home a few key points to what makes

Allegiance different from other carriers, whether it's an (indiscernible), an LV Carrier, or any of the emerging telecom companies in general. No other company is really set up to address the small or medium-sized businesses like Allegiance. First point clearly is our address to the market. With 789 (indiscernible) billed across 36 markets, we actually have a larger footprint than any of the R Box (phonetic) or ILEX (phonetic) in the country with up to 20 million access lines up for grabs for small and medium-sized business. You know in January, because of the scaling of the factory, we for the first time launched a product offering that really plays to the strength of allegiance. No. 1, the first product offering that we went to market with is Allegiance Select. Let me explain what Allegiance Select does. Allegiance Select is a product that

targets multiple location companies. Here's how it works:
any company who selects Allegiance for both their local and long distance can call between these offices for free. For example, if ABC Company has a location in New York, a location in Portland and location in Los Angeles, oftentimes these branch offices or relocations need to communicate with each other. By using Allegiance Select they can call each other for free. No other carrier is set up to do this on a national basis. We're the only true national local provider. The cost for transport between our switches for long distance to Allegiance is roughly about half a cent a minunt because essentially we own the local service lines on each of the call. Meaning the originating and terminating end of the call is all hosted and held by Allegiance. We have a huge cost advantage over the regional players who typically would only be servicing one location at a regional basis. The LD carriers really can't do this on a national basis because they depend on a local service provider to get on and of their network. The second significant product offered that we did, we decided to lower the entry point for I-A D, which we call total communications from 8 lines of voice and 256 K of data down to six lines of voice. And the reason we're ready to do that is simply the factory is scaled up to the point where we can handle demand. I would have done it much sooner but we couldn't keep up with sales initiative to install everything that we could sell. Well, we finally feel that we have scaled the ramp the factory tp the point. What this does for us as a company is it enables us to address another segment of the market wherein the past I would sell them strictly UNIS, I wouldn't be able to give them a significant data offering, and now suddenly each time we make a sale of a six line voice I'm suddenly picking up a 256 K a day data to boot. And some things that you need to think about, the differences between the I-A D customer base and the UNI customer base. No. 1, all I-A D total communication customers are under long-term contracts. It can be a one year, two-year contract and they all have teeth with a revenue commitment. No. 2, (indiscernible) on a IAD TC platform has historically been lass than .5 percent per month simply for a couple of reasons. No. 1, Bell doesn't go to market this way. No. 2, when we launched the company we realized that we had to the market and make it simple as a me to strategy of Bell. Today with Allegiance, I-A

D and Allegiance Select and total communicate with a six line entry point, Bell really has no offering That is a threat to this product. We have a direct sales first addressing the marketing, Bell does not. Bell does not sell IAD or TC. Bell does not bundle an LD, hosting e-mail, data, local voice all one same line, all on the same bill. And finally, Bell does not serve customers on a national basis. That's the reason they are called regional Bell operating companies. Bottom line: Dell does not have an answer to TC, I-A D or Allegiance select and that's why we have been so successful with it. And No. 2, Allegiance as a stand-alone company is finally playing to its strength with its national footprint. Royce, take it away.

MR. ROYCE HOLLAND:
floodhas discussed our results for the fourth quarter and for the full year 2001 and Tony has talked about the huge progress that we've made in scaling the fastest-growing segment of our business, integrated access service. And I think this is critical, the scaling of that business to us having a very very good year in 2002. I'm going to provide some additional color to 2001 and provide our guidance for 2002 as well as provide some updates on our BackOffice system upgrades and the 2002 regulatory agenda nationwide. But first, I'm going to put to bed some of the wild, crazy and irrational rumors and witch hunts that have been raging like an Idaho forest fire in the middle of a fifty-year drought. Now, whereas most of these have not been specific to Allegiance or tied to us, still the overall climate out there has had a bad effect on everyone, and the genesis of these rumors is not just overal economic climate which we all know has been difficult for most industries since the tragic events of September 11th, but it has been exacerbated by the Enron debacle as well as recent bankruptcy filings in the Telecom industry by global Crossing and the clouds, plus many of the rumors swirling around WorldCom, Williams, Crest and others. While I cannot really comment on the validity of these rumors as it affects some of our peers out there in the marketplace, I can demonstrably comment on their effect or their lack of effect on Allegiance Telecom. First, with regard to what I call the accounting and financial flavor of of the rumors. Unlike Enron, Allegiance has no off-balance sheet financing. Our debt structure consists of two high yield bond offerings, a bank facility and capital leases in to 50 to $60 million range. I know it's boring, but that's it. Two, unlike Enron, we have no bond rating triggers. Three, unlike the rumors about many other telecom companies, we are in compliance with all of our bank covenants and we plan to stay that way and I will discuss this further when I present guidance for 2002. And unlike Global Crossing,Quest and other, we don't sell IRUs and we have not done any capacity swaps. A round-trip to me is taken on American Airlines, not in the accounting books. Unlike some who are facing investing write-downs, we have no minority interest in other entities other than a very nominal investment in Jump.Net which was an ISP in Austin Texas that we acquired in 2000 that has a couple of minor investments in some other service providers in exchange for services that they provide. We also have no strategic relationships requiring present or future

capital commitments. Like some other Telecom companies, we do use Arthur Andersen as our auditor and they do our audit but they do an immaterial work for us related primarily to tax matters and they do not do internal audit or consulting work for Allegiance. The Andersen audit team has assured me, the team assigned to our account, has assured me that they have no connections to the work that Andersen does for Enron or any of the other problem children out there. With regard to the Allegiance staff, we have one staff account that has worked for Andersen in the past. Our Chief Financial Officer, our Senior Vice President of Finance and our Comptroller our top three financial officers, have never worked for Andersen. Many of these things I guess you'd said they are pretty clever tricks to fool investors and some folks have done that well. I think Tom and Clay and I just are not that clever, so the rumor blunders -- I think you're going to have to look for a more exciting target when it comes to getting into the accounting and finance books. The next area is insider relationships with the Company. I'm pleased to say that unlike Enron, we have no special purpose subsidiaries and no business entities with ownership by Allegiance executives or any other employee for that matter. Now many Allegiance executives and employees are investors in Allegiance but it's all solely at the parent company level through common stock ownership, aligning our interests with those of our shareholders. In fact, Allegiance has one of the largest percentages of the executive and employee ownerships in the Telecom industry and I think that's a good thing. And finally, unlike some of the other players that we are aware of out there, the Chairman and CEO of Allegiance, yours truly, has not reaped hundreds of millions of dollars from selling company stock and he has not borrowed hundreds of millions of dollars from the Company. And in fact he has never sold a share of Allegiance stock and I that definitely puts both his sanity and his greed at question, I recognize, but on the flipside, he has no debt. Doesn't owe money to Allegiance or anyone else. My fanaticism about a strong balance sheet extends to my personal finances and it does not take a rocket scientist to figure out that I am highly motivated to make Allegiance Telecom a rip-roaring financial success, myself and all of the other people sitting around this table who are also owners. Now let me get to the year 2001 performance. Now that I'm belaboring the obvious, the 2001 in many ways presented the toughest business environment since the 1973-74 period, which was dominated by Watergate, soaring energy prices and high unemployment and inflation. In 2001 the economy went into a recession which was exacerbated by the tragic event of September 11th. Things we were even worse in the Telecom sector, wherein the shakeout of new inputs became a flood and even the largest, most established players were plagued by low, single digit topline growth rates and very low earnings growth. Despite the capital markets equivalent to nuclear winter, I feel that we turned in a very solid performance, as we completed our 36 market buildout and still maintained high octane topline growth and began to move down the path to profitability. Now, let's take a look at our 2001 report card. Comparing our 2001 performance to the target that I articulated in our

conference call last February, first, in terms of net worth deployment, we stated that we would bring our remaining nine markets online in 2001, and indeed we did that. We also predicted that we would install sonic fiber rings to replace (indiscernible) capacity and that would be in 19 markets by the end of 2001. We actually exceeded that, we were at 22 by the end of 2001. We forecasted net installs of over 500,000 lines for 2001 and made that number our actual performance was in the range of 525 to 535,000 net installs. Our target revenues in 2001, we predicted 550 million, which represented a 90 percent growth rate over the 285 million in 2000. Our actual performance on the top line was a little short at 517 million, although that still represents an annual growth rate of over 80 percent. As we previously discussed, the reasons for the small shortfall are twofold: the main reason is our decision at midyear, which we talked about in Q3, to discontinue growing our high-end Web hosting business due to industrywide overcapacity and poorer margins in the (indiscernible) location and large dedicated hosting areas. We continued to grow our shared hosting primarily through rapidly growing our integrated access products. The aftermath of September 11th and its impact on sales and installs in September and October also accounted for a smaller amount of this revenue shortfall. In terms of EBITDA, however, we forecasted improving on our $118 million loss in 2000 and improving that to the 100 million to 105 million dollar range in 2001. Well, despite our small shortfall in topline growth, for the reasons we discussed, we almost managed to hit our EBITDA forecast coming end of the loss of 107 million for the year, excluding non-recurring acquisition accounting adjustments that we talked about before. This is a clear indication of better than forecasted margins at our retail small and mid-sized enterprise business. Even more significant was the improvement in the EBITDA loss margin from 31.5 percent in Q4 of 2000 to 14.6 percent in Q4 of 2001. CapEx for 2001 was forecasted at 350 million. Actual CapEx was slightly higher at 365 as we are forecasted with the year, due to the additional sonic rings being lit in three additional markets and the upgrade of our Internet backbone to OC 48 (indiscernible) of wavelengths connecting our largest markets. That was truly a target of opportunity on pricing to move ahead. In summary, we are pleased but not satisfied with our 2001 performance. We were essentially on plan for all of our major parameters except revenue growth which was slightly shorter plan due primarily to what I feel was a very prudent business decision not to pursue a significantly diminished business opportunity in high-end Web hosting. Even at that, I (indiscernible) a growth rate of over 80 percent in this type of market environment is not too shabby. Four, moving on to our forecast for 2002, which we expect to be marked by continued (indiscernible) topline growth and the achievement of a significant milestone for this or any other enterprise and that's hitting EBITDA positive in the second half of the year. In terms of net installs, we're forecasting about 600,000 net new lines to be installed in 2002. I'd say that's plus or minus 25,000. As we have previously stated we expect revenue to grow to about 800 million, an annual growth rate of over 15 percent, still very robust growth. We

have not provided quarterly guidance up until now, but now I am going to do so. Also, as Tom pointed out, there is a lot of heightened interest out there in compliance with debt covenants and I will repeat those as I talk about our quarterly revenue forecast. In the first quarter we're forecasting revenue to be in the 165 to $168 million range vs. the covenant of 155. In Q2, the forecast is 185 to 190 million with a covenant of 180. In Q3, the forecast moves up to 208 to 213 million with a covenant of 200 million and Q4 has a forecast of 232 to 237 million with a covenant of 220 million. We feel that we will be in comfortable shape just like we were in 2001 on making those covenants. Our forecast results in continued higher octane topline growth of about 10 percent quarter over quarter in our annual growth rate in excess of 50 percent. That compares to forecasted annual growth rates in the low single digit range for our major competitors which are the regional Bells and the large interexchange carriers. We also are comfortable in our ability to stay in compliance with our debt covenants, as I pointed out before. We have previously provided guidance that at these growth rates we will be EBITDA positive in the second half of 2002 and we are reaffirming this forecast today. We also forecasting a cumulative ebt in the range of 15 to $25 million for the year versus 107 for 2001, with the first half of the year providing the losses and the second half of the year providing the gains. We expect the cost that EBITDA breakeven threshold about the start of the football season, sometime late in the third quarter or early fourth-quarter. We previously forecasted CapEx for 2002 to be in the 225 to $250 million range, with the completion of our budget, we are today lowering this forecast to a range of 215 million to 240 million, resulting in slightly improved capital efficiency. The bank covenant for this is a maximum CapEx as Tom pointed out of 400 million and we're certainly confident that we will be in compliance with that. As we've discussed on many occasions, the two major foundations of our success are our financial strength and our world-class BackOffice systems and processes. Tom has discussed the former and I'll updatd the latter. Our BackOffice support systems as they're commonly known, have been a constant work in progress since they won as we continue to replace manual processes with automation, continue to promote electronic bonding with the ILEX and develop system interfaces to monitor our work queus, improve processes disability and database integrity and consistency. In Q4 and continuing into Q1 of this year, we've achieved milestones in some of these areas. First, we implemented the saddle billing system, the single view system referred to in the press release for one of our new cities, Pittsburg and for new customers in Philadelphia. In Q4, and we did this in Q4 and the results are excellent. We expect to be implementing saddle for new customers on a market by market rollout from now until the end of the third quarter. I know many of you are rightfully identifying any billing migration as a risk area but bear in mind that for now we're doing this for new customers in existing customers leaving existing customers on ability and the results so far I'm pleased to report that this risk is being very well-managed by our IT and our billing teams. In the second quarter of 2001 we reported to you that we had

rolled out an automated billing interface. We call a BIF, for our unbundled loop customers between our provisioning system and our legacy billing system, the ability (indiscernible). The elimination of the manual keying of billing information into ability had two huge benefits: one, it eliminated the lag time which sometimes had been over two months in getting out a new customers first bill due to all the manual processes. And even more importantly, it virtually eliminated data entry errors in the billing on a going forward basis. In the fourth-quarter, we've extended this same type of BIF to the saddle single view platform as we brought it up for the first two markets for unbundled loop customers, Philadelphia and Pittsburgh. These are major accomplishments but the job is not finished. Two more systems still require manual keying of the data into the billing systems. The new customer orders for integrated access and other TI based products and (indiscernible) orders for all prospects and customers. Until recently, development of an electronic interface for integrated access was not as critical, but as Tom pointed out, our sales for T1 based products equalled unbundled loops in Q4 and our forecast for 2002, at Tony indicated, are that a the majority of our new installs will be integrated access or T-1 developed voice and data products. The (indiscernible) process has always been a challenge, some call it can of worms, for most telecom carriers and we are no exception in that regard. Most of our MacB be problems have really been a result of too many manual processes and certainly a (indiscernible) between provisioning and billing would be helpful in that area. I'm pleased to say that the fix is almost ready. As I speak we're testing electronic billing interfaces between provision in both the ability and saddle platforms for T-1 delivered products and for disconnects. The (indiscernible) and changes interface is still in development. We expect most of these BIF's to be of service both for the new orders for T-1 and for disconnects and the manual keying of new installations and disconnects in the billing will cease at the end of February. Coincidentally, with the development of these systems in the fourth-quarter I commissioned a long overdue in my opinion database reconciliation project to reconcile our order management provisioning and billing databases for the inconsistencies that had developed over the years due to manual data entries into the system and also due to minor differences in the way we count lines in our various systems. For instance, in order management system we use more of a DSO equavalent bases and in our billing systems we use something probably a bit closer but certainly not quite the same as the ILEX. I think we do a pretty job of counting voice but we don't count data equivalent lines particularly one of those that are understated. As part of the reconciliation project we also appempted to reconcile the provisioning and billing databases for the small portion of our business that includes resale services for offset customers. Many of these have been around for awhile. This is a more difficult task since we are dependent on the ILEX (phonetic) for delivery of product and billing information for resale and that really clouds our visibility with regard to lying count, though not really to revenue. As a result of the reconciliation we are adjusting the line count downward in order management

system, which is the basis for tracking lines, by about 125,000 lines to be consistent with the line count in our more conservative billing systems, which really are the ones that we calculate our RPU (phonetic) based on (indiscernible) revenue. This adjustment is broken down into 95,000 facilities based lines and 30,000 resale lines. Going forward, we will use a standardized line count methodology between the systems that is much more similar to the billing system. After final adjustments and lock down of the various systems the percentage of facilities based lines increases to 93 percent, due to a lot of the resale lines that we took out. Since the inconsistencies, resale lines or should say, since the inconsistencies between the various databases had a nonmaterial and we certainly define that as $5 million or less impact on revenue, you would actually RTUs (phonetic) increase to over $50 per line as Tom pointed out, based on using the billing system accounting methodologies. Another project that we are really gaining traction on and a lot of work was accomplished in Q4 is our electronic bonding of trouble ticket systems with FBC communications being our first partner in this area. This is a tremendously successful project. It's finishing data testing and will be rolled out at the end of February, and it will illuminate the telephone tag that often occurs when we and FBC or other ILEX (phonetic) are working trouble tickets. This will be an electronic interface that will allow us to exchange trouble ticket information and updates with FBC on a real-time basis and also allow us to keep customers up-to-date on the status of trouble on their voice or data lines in real-time. This has been very successful. Just like we did with our provisioning electronic bonding, we plan to take the good work that FBC andbusiness have done and try to use this as a model to facilitate trouble tickets bonding with our other ILEX (phonetic) across the country. Moving on to the regulatory agenda, I think that what you're seeing in 2002 is a lot of pomp, probably the circumstance will not measure up to the pomp. I think we will see a lot of activity, a lot of voices and words being generated, perhaps not a lot of action, and probably not a lot of significant change in 2002. I think you will see primarily a fine-tuning of the Telecom Act of 1996. In Congress, we've got almost a stalemated situation in telecom. The House and Senate commerce committees are at polar opposites with respect to the main telecom players. In the house, the two ranking members of the commerce committee are really pushing the Bell company agenda and in the Senate, the ranking members of the Commerce Committee are pushing the competitive agenda. I think it is possible the infamous Toes and Dingle (phonetic) Act which would constitute a major rewrite of the Telecom Act and would really be to the benefit solely of the four Bell companies, is due to come up for a vote on February 27, and it might actually pass. It will not in our opinion go anywhere in the Senate. I think what you're going to see is with regard to Capitol Hill, you going to have the normal gridlock associated with Washington in telecom like you see with a lot of other things, and that's fine with us if that happens. I think the FCC, we will see some results there. It has a lot of notice of proposed rulemaking vowed as a result of the tri-annual overview. It's hard to imagine that it's been six long years since

the passage of the Telecom Act, but we are to the second tri-annual review. My expectation is that we may see some better performance metrics identified. We've hard a lot of talk about better enforcement from the FCC. I think will see progress in that area. We may see some restrictions ultimately put on local switching, where that starts to be phased out for certain classes of customers in certain urban areas, but I think what you're going to see is an evolution, not a revolution, and we're going to be continuing to conduct business as usual. Well, in summary, this has been--2001 was a very interesting year. I know the legendary investor from Omaha, Warren Buffett, recently wrote in Fortune magazine, the tour we've taken through the last century proves that market irrationality of an extreme kind periodically erupts. I think here in the new century, few investors, either Allegiance investors or other, would argue with the fact that we've almost in one of those constant periods of irrationality, both on the upside and the downside for the two years of the new century. Well, despite this challenging business market, I feel that 2001 was a year of significant accomplishments and milestones for Allegiance, rolling out a 36 market, posting an 80 percent topline growth rate and improving margins. Although we're not immune to the irrational valuation distortions of the capital markets, we have avoided the liquidity crisis, over leveraged capital structures, falling demand for services and overcapacity problems of much of the industry. And while many of our peers and competitors in the industry blame their lack of success on the economy, on the regulators, on changing technologies and changing market conditions, we remain confident. And this is important, that we can continue to execute our business plan and achieve success, even in capital the market's equivalent of nuclear winter. We plan no restructurings, no clampdowns and no other forms of financial engineering, just continuing to execute our plan and conduct business as usual at Allegiance Telecom. And when nuclear winter in the capital markets ultimately yields to a more traditional financial environment, which we're all eagerly awaiting, I am very confident that a profitable, high-growth financially strong enterprise can build tremendous shareholder value. And everyone sitting around the table at Allegiance on the management team that is an investor is certainly signed up for that happening. Thank you very much for joining us and now we would be very pleased to answer any questions.

THE OPERATOR:
(CALLER INSTRUCTIONS) Our first question comes from Jim Friedlan (phonetic) with Robertson Stephens.

THE CALLER:
A couple of questions. No. 1, in the first nine markets, in terms of sequential growth, it seems it was a little light compared to the rest of the Company, and also that EBITDA margins ticked down a little bit. I was wondering, first, if that just includes a non cash item but also what's going on in the core markets in terms of growth there? And then if you could just give some overall comments

on pricing and competition. Are you seeing fewer people out there, and especially as it relates to ARPU (phonetic), what are your assumptions going forward in order to make the numbers? And I guess the last question would be, in terms of guidance, does the guidance assume any improvement in the economy or the environment, or is that just sort of your run-rate operating levels that you are seeing?

MR. ROYCE HOLLAND:
Let me grab your last question first. As far as guidance, that guidance does not assume an improving economy. As I say, we've been in this--I think in the telecom area, this capital market's equivalent to nuclear winter, really since October of 2000, and even though we're tired of it we're ready to see it go away, and I'm sure I speak for the whole industry and all of our investors. We don't control that and we're not shaping our business to accommodate that. In terms of pricing and competition, I would tell you that there's been in the market we are in, our core business, the SNE retail market, there's been very little price changes. Competition still is primarily with the ILAX (phonetic). I mean, we used to say in the past, I know two years ago when the markets were in a frenzy and everyone was getting financed and there were hundreds of CLAX (phonetic) and other emerging telecom providers. On this call I got the question, which I got probably 100 times on calls and road shows, how is Allegiance going to get 5 to 10 percent market share and be successful when 20 other players out there are planning to do the same thing? You know, I haven't had that question in a long time because I guess those other 19 probably are not around anymore, and they're kind of limping, and certainly we do see less competition in the market today because there are fewer players. Although even back then we saw more competition from the ILAX (phonetic). That was our primary competitor at the low end of the market. Where you do see more competition from the ILAX (phonetic) is at that the low end of the market. If it is a one or two or three line customer that is voice only, like a beauty shop or something, it's a price sensitive market. The (indiscernible) win back programs do have some success. As you move up market a little into the service industries that take the product that Tony talk about, which is our fastest-growing product and we'll comprise the majority of our new business this year. That is a very nonprice sensitive market. That is a very feature sensitive market. It's really driven more than anything by the migration from either a dial-up or low speed dedicated connection for Internet access to a high-speed dedicated connection. I'm not talking gigabit Internet I'm talking 256 kilobit up to maybe a T1 on the top end along with bundling the voice service website domain registration, e-mail and the works. And that's not a competitive market. So in terms of the competitive landscape, you know it really has not changed a lot. In fact, from our standpoint, where you are in the market, you're being successful is probably less today because so many players that have gone away. With regard to the first nine markets, what you see on that particular page is a direct reflection of us doing our database

reconciliation. As you can imagine, I talked about taking out 30,000 resale lines, those 30,000 resale lines were just about all in those first nine markets. Also, I talked about all of the reconciliation basically had a nonmaterial effect, you know 5 million or less, on overall revenue in the fourth quarter. Nearly all of that was in the nine markets. So what you saw was really an anomaly due to us getting our systems cleaned up as a result of us putting in this series of automation to where we eliminate these problems going forward. So I wouldn't really draw any conclusions on any trend from Q3 to Q4. Q1 you will start to see the trends I think moving in the direction that you are accustomed to.

THE CALLER:
Great, thank you.

THE OPERATOR:
We'll now hear from Peter DiCaprio with (indiscernible).

THE CALLER:
I was wondering, the additional market that was opened up in the fourth quarter, what the associated or if there was any additional EBITDA expense associated with that? And also curious, I guess maybe for Tony, if the 60,000 installs this quarter are a little bit of an anomaly --or the 60,000 installs in January are those a little bit of an anomaly or is that kind of a run-rate that we should expect for the full first quarter?

MR. ROYCE HOLLAND:
Let me jump on the second one and then I'll hand it to Tony and then Tom can (indiscernible) the first from Peter.

COMPANY REPRESENTATIVE:
No, I don't think it was an anomaly at all. The thing I want to point out to you is, I gave you 60,000 lines, that was only the month of January and that was only unbundled loop and the Broadband products. That does not take into account some of our other product offerings. So I'm banging the table saying, "get ready, it's coming". Tom, do you want to do the other one?

MR. THOMAS LORD:
With respect to EBITDA, I told people this consistently, yes we take it in the shorts every time we open up a new city or two. It's a strategic decision. One of the things we did to try to stay inside the cash envelope (indiscernible) as Royce talked about, when things changed and we took our own small knife, no a large machete, to the SG&A side, is to weaken effect the cash envelope in spite of where ever there might be revenue weaknesses and stuff. But the fact that we had one city that was an extension city let say, may the EBITDA loss in the Boca Raton West Palm Beach area, much less egregious on the negative side as

compared to when you go into a city which has, call it an island, in Pittsburgh and you've got to open up the switch to people, the train and the entire enchilada. So, Pittsburgh definitely cost us more than Boca Raton but we have high expectations for both cities. I guess the good news is now that we're not opening up any new openingm, we're not growing cities, we're not acquiring cities, were going to do any that stuff that we can see right now until the capital markets come back and even then I'd have to question the sanity if we wanted to go do that. I think that the EBITDA drag will continue a little bit into the first quarter and then you are going to begin to see some fairly dramatic leverage in Q2, Q3 and Q4.

THE CALLER:
So, the Boca Raton West Palm market, was that originally scheduled for the first quarter of 2002 and you guys bumped it into Q4 '01?

COMPANY REPRESENTATIVE:
No. What we did is we changed couple of cities around that are going to be what I call island cities, and decided to really extend the market. If you look at the city of Los Angeles, it's it's state. If you look at Florida, I'm a resident of Miami, from Homestead, up to Boca Raton and West Palm Beach, it's a very eclectic community but I call it the city of I-95 South and so you can have multiple markets inside of these areas. We decided that was a more efficient use of capital that it was to try to go off and do let's say another independent city like Milwaukee or something. (indiscernible) Under consideration, just to add to that, I think that is something that a lot of folks don't appreciate, that the energy and the expenses that you incur when you are rolling out almost a market a month like we've been doing the last three years. And headcount keep adding the (indiscernible), the network expense and everything else. In the fourth quarter of this year there's an interesting statistic: we have a revenue per employee of $150,000 per head annualized, taking the quarter revenues and annualizing them. That was up from 135 I think it was in Q3. Well, bear in mind that headcount will stay fairly close to constant this year because we're not rolling out new markets. So we will be in the 4000 to 4300 range on headcount for the full year and we're planning to do 800 million in revenue, and our run-rate in the fourth quarter of this year is going to be up over $900 million, as far as a quarterly revenue run-rate, that's going to put us up somewhere in the neighborhood of $225,000 annualized per employee. That's the type of leverage that's very very inherent in leveraging salary and head count related costs of the SG&A and that's the main type of driver you are going to see moving us to EBITDA profitable in the second half of the year.

THE CALLER:
Tom, what do you think the impact was on the additional market on the EBITDA in the fourth quarter?

MR. THOMAS LORD:
Peter, If I knew that number I would give you an answer but I honestly don't.

THE OPERATOR:
We'll now hear from David Farden (phonetic) with J.P. Morgan.

THE CALLER:
Congratulations on the quarter. I just want to follow up on couple of things. I have to tee up for this one. The nonzero revenue impact from the intermediate deal, I mean there has been a lot of questions in the mark about whether or not that's in or will be in or is out of the guidance that you guys are giving, the 800 million, the quarterly ramp up that Royce gave us. So if you could just give us a sense of when we do get it, is it going to be added to the numbers that we're seeing? And then I have a couple of just detailed questions. One was on the SG&A write-off. Could you give us a sense of what was the reason why the 11 million was in the numbers as reoccurring charge reserves but the 5.5 million was not part of that charge, somehow separated? And then lastly, on the issue of looking at the quarterly guidance, we're obviously looking for a pretty substantial ramp into Q2 and maybe this falls to Tony a little bit, but can we compare and contrast where things are now in the fourth quarter, the impact of September 11th, the impact of opening new markets, etc., and where we're going to be in the second quarter in terms of the level, the ramp we're talking about? What's going to change between Q4 and Q2 that we can keep track of to get ahead of time that the numbers are going to be what they are supposed to be?

COMPANY REPRESENTATIVE:
In terms of the IBI guidance, I think that any investor on this call, our bank credit partners, high yield community, the equity community would find me to be an insane, mad, rating, foaming at the mouth individual if I was to hop on this call and take guidance up. I have not heard one telecom company take guidance up. So I'm not going to the first moron that you all nominate for fool of the year, okay? The strategic issue, however, you still might want to nominate me for fool of year for working here, but the strategic issue that we're dealing what is that, and I do the same thing you all do, I sat in your shoes. If you go back and look at what DigEx (phonetic) was and what WorldCom has, some people call me up and say they thought this was a two hundred million dollar a year animal. If it did $200 million a year I guarantee you we wouldn't be doing 800 million dollars. But the bulk of the revenue stream that is inside of Intermedia was of not much interest to Allegiance. I don't want to say that in an insulting fashion to customers we're going to try to keep, but you know I have a fanaticism about getting paid. And the net z's and the net zeros and the people of that ilk that had credit problems, we don't care to have them dump their creditworthiness on my pristine balance sheet. And so, Chris Malinowski, I sat down with them, the

whole management team asked me and said, go look at each one of your accounts, retail. On an account by account basis, accessive profitability, specifically first those are OnNet and the look at the ones that are off net. In terms of the wholesale side of the business the stupidest thing I could do would be to put myself in a very awkward box and that would be go grab a sh*tload of revenues that are not going to stick, that we know are going to turn off and go away, so I'm going to reserve for those as we go into Q1 and Q2 and Q3 and not set myself up for a fall in 2003. Of all the acquisitions we make, every acquisition we've made to date with the exception of IBI were driven for one thing: an install customer base and a sales team. That brought revenues with it. The principal driving motivation factor behind IBI acquisition was to establish ourselves as a Tier 1 IP piering provider as a result of the organic growth that Tony has been delivering on integrated services access offering. We would have still acquired this asset if it had a revenue base of zero. So the entire focuse in terms of the purchase contract and everything that we worked with with WorldCom, who I have to say were great business partners in working with us, with a gun pointed at their head called the Department of Justice in terms of having to unload this entity, was simply to make sure that we had a handle on the cost structure, inside it, and that we've effectively had true (indiscernible) with their very very valuable asset (indiscernible). So when I say nonzero number, I mean a nonzero number. I don't know what it is right now. If I had that type of insight I would be retired at the beach. But what I have said to people is that after we've owned and run the enterprise for about six months, I think we will have a handle in terms of what it's going to be. The other thing that I can tell you, this is kind of interesting, is that I asked Chris after he'd gone through and looked at the names of some of the customers and I talk to Tony, and I said, lets see if there's any overlap in terms of existing IBI customers that were being targeted with sales proposals and quotas from Allegiance where we were going to basically go off and compete with that organization in terms of the success we were having with I-A D. We were surprised to find that we were either going to go get the business through a sales call, in coming in with the integrated services offering for the full envelope, or we were going to end up owning the customer as a result of the acquisition. So the fact that you got a lot of wholesale that we don't think we will keep, we know where the DigX (phonetic) revenues are going to go, and that there was some overlap in terms of the OnNet cities that we serve as targeted customers for what we're doing. The revenue contribution that I expect it will receive from IBI for from the year is not going to be that great. I amd glad I'm going to have some but it's not something that I've really dialed in on. In terms of the sgna write-off from an accounting convention perspective, the $11 million that we took was exactly how Clay and I've gone about in the past. Some might find it to be to high or to larger of a number, but if this economy comes back and bites us in the ass which we're not looking at happening, I want to be protected for a downturn even though I can't see that downturn. We can specifically identify things that were

not part of the normal accounting that we do that were inside the acquisitions we've made, some of the things that Royce as talked about, in terms of these data reconciliations, we found some billing systems that were inside some of the companies that were in the process to be migrated. I could have continued to have amoritized that over the balance of 2002. I think in this day and age, the favorite word I here is, in this environment. I wanted to air on the side of being overly writing off, overly expensing, overly finding kitchen sinks and overly witch hunting myself, overly microbiologing my own balance sheet and P&L, so that we would be able to present to you in the fairest light the Company's financial picture. In terms of the Q2 ramp, Tony you're up.

MR. ANTHONY PARELLA:
Couple of things I would say is changed since September 11th. Number one, I believe the sales ramp is back to full steam. There was some drag over into Q4 and wasn't necessarily that the new demand was not there, but that some of the backlog had aged as a result of not installing in September and early October in certain markets and that caused a bit of bigger cancel rate than we normally would have experienced. That's clearly behind us based on what I've seen in January and the early part of February. On the install side, I feel very confident that we have the factory of Broadband ramped up. It took us a year to really scale this thing and get the process down and the field organization trained from an install perspective. It's just not something you can turn on a dime to scale. I think we finally have scaled it to the point where I fully expect IAD to become a bigger line contributor but more importantly revenue contributor over the next year, to the point that right now they are running at about 50 unis (phonetic) versus IAD. I wouldn't be surprised to see it ramp up 6040 by year-end, and that translates into higher revenue per customer, certainly less churn because there is no wind back against it. So I think that makes it better. The other thing that I just want to add that is not really tied to September 11th but it is an issue, with all of the failures in our industry, there really is no one nationally competing against us, and with this Allegiance Select again, and the six line entry point with voice with 256 K. of data, I feel very confident that we've made the shift of being a me too player of Bell to really leveraging our strength of all these years building the foundation of this company. I'm very optimistic. I think it's going to be a good year.

THE OPERATOR:
Thank you gentlemen. At this time there appears to be no further questions.

MR. ROYCE HOLLAND:
Yes, I know we've unfairly long today, I want to thank you for hanging in there with us, with this being an end of the year type conference. We had a lot of information to get out. I hope it is very helpful to you, for our investors and for

our analysts we certainly hope a very successful and profitable 2002 awaits you as it does us. Thank you very much.

THE OPERATOR:
This does conclude today's conference. We thank you for your participation. (CONFERENCE CALL CONCLUDED)

FDfn

FAIR DISCLOSURE
FINANCIAL NETWORK

EXHIBIT C

Analysts' 2002 Revenue and EBITDA Estimates
Before and After the February 19, 2002 Disclosures
($millions)

Date	Firm	Prior 2002E Revenue	Revised 2002E Revenue	Difference	Prior 2002E EBITDA	Revised 2002E EBITDA	Difference
2/19/2002	CSFB	784.40	769.60	(14.80)	(30.70)	(35.20)	(4.50)
2/19/2002	Salomon Smith Barney	780.00	780.00	-	(13.00)	(25.00)	(12.00)
2/20/2002	Baird	800.00	785.00	(15.00)	(20.00)	(20.00)	-
2/20/2002	BB&T Capital Mkts	814.70	800.10	(14.60)	(6.20)	(25.00)	(18.80)
2/20/2002	Bear Stearns (FI)	781.20	781.20	-	(22.30)	(22.30)	-
2/20/2002	CIBC	785.00	785.00	-			
2/20/2002	Deutsche Bank	770.00	774.30	4.30	(28.00)	(29.00)	(1.00)
2/20/2002	Goldman Sachs (FI)	785.60	785.60	-	(12.30)	(12.30)	-
2/20/2002	Hibernia	807.60	807.60	-	4.50	(3.90)	(8.40)
2/20/2002	JP Morgan	801.50	801.50	-	(19.40)	(19.40)	-
2/20/2002	Lehman Bros.	783.50	773.30	(10.20)	(7.20)	(16.60)	(9.40)
2/20/2002	McDonald	789.10	775.00	(14.10)	(45.40)	(29.00)	16.40
2/20/2002	Robertson Stephens	803.10	771.10	(32.00)	(10.00)	(23.90)	(13.90)
2/20/2002	Stephens Inc.	802.84	799.81	(3.03)	(0.40)	(22.08)	(21.68)
2/20/2002	Thomas Weisel	824.90	824.90	-	1.70	1.70	-
2/20/2002	UBS Warburg	785.00	785.00	-	(21.00)	(21.00)	-
2/20/2002	US Banc Piper Jaffray	800.00	800.00	-	(16.90)	(16.90)	-
2/25/2002	Kaufman Bros	768.50	774.60	6.10	(29.90)	(24.20)	5.70
	Average:	792.61	787.42	(5.18)	(16.26)	(20.24)	(3.98)

EXHIBIT D

Allegiance Telecom, Inc.
Daily Stock Price and Selected Events
April 16 - June 28, 2002

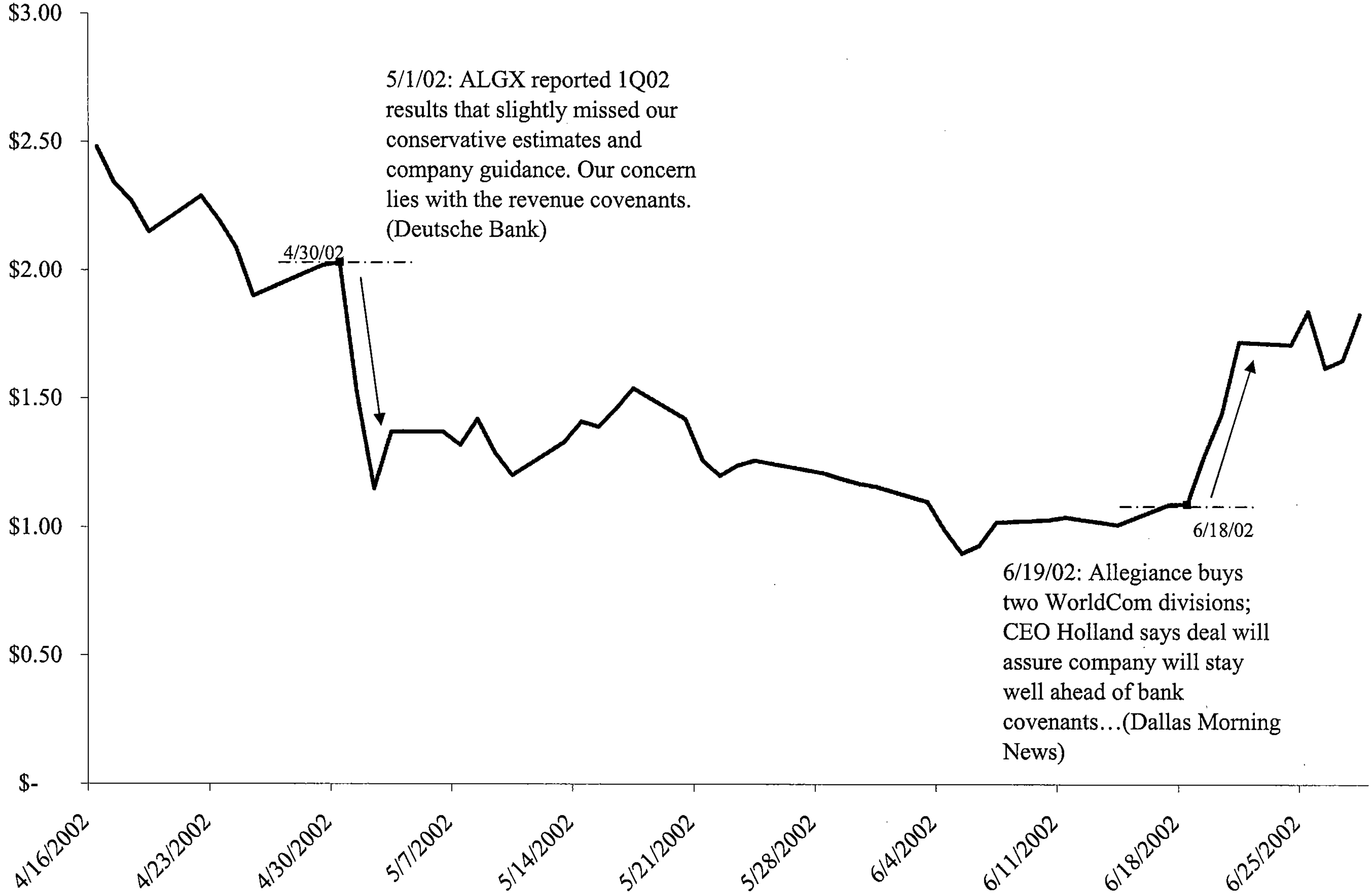

EXHIBIT E

Allegiance Telecom, Inc.
Daily Price vs. Nasdaq Composite Index and CLEC Company Index
January 2, 2001 - May 31, 2002

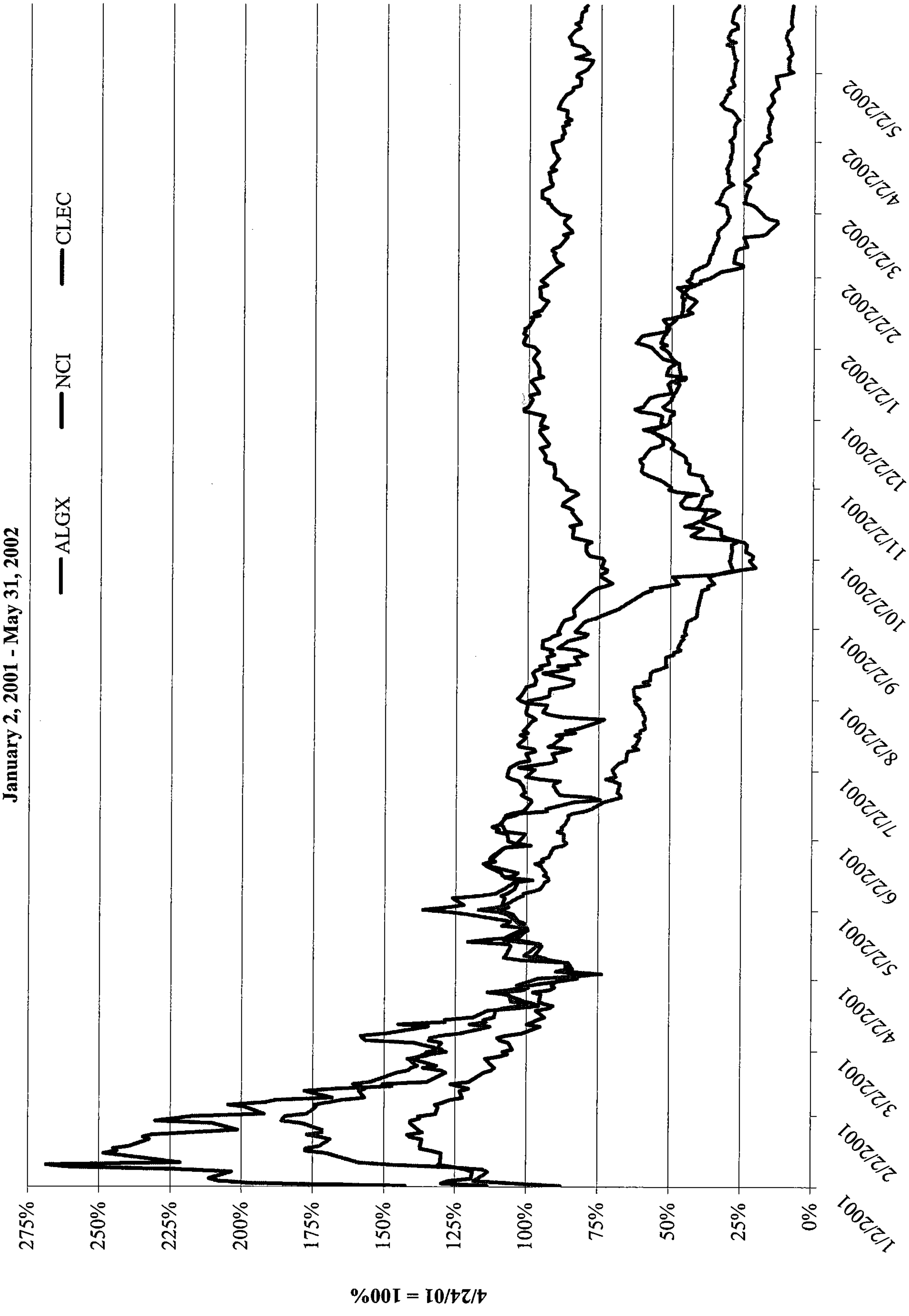

EXHIBIT F

PRN Allegiance Telecom Announces Double Digit Sequential Revenue
Jul 30 2002 16:01

Growth And
Improved EBITDA and Cash Burn in Second Quarter

- 2Q02 Revenues of $184.4 Million, Resulting in Annual Increase of 48.7 Percent
- 20 Markets Pre-Overhead EBITDA(1) Positive in 2Q02
- Approximately $10 Million Improvement in EBITDA from 1Q02 with EBITDA Loss Margin Reduced to 6.4 Percent in 2Q02 from 13.4 Percent in 1Q02 (before giving effect to charges related primarily to WorldCom exposure in 2Q02)
- 14 New Colocations for a Total of 829, Addressing Approximately 21.63 Million Business Lines "On-Switch"
- Record Gross Number of New Installs With Net Installs of 106,700 Lines including Disconnection of 58,000 Qwest Wholesale Lines
- $354.0 Million Cash On Hand End of 2Q02
- 2Q02 Capital Expenditures of $42.4 Million, Reduction of 63 Percent From 2Q01
- Acquisition of Customer Premise Equipment (CPE) Provisioning and CPE Maintenance Businesses from WorldCom
- Draw Down of $135 Million in Funds Under Senior Credit Facility

DALLAS, July 30 /PRNewswire-FirstCall/ -- Allegiance Telecom, Inc. (Nasdaq: ALGX), an integrated communications provider (ICP), today announced results for its second quarter 2002. Allegiance reported second quarter revenues of $184.4 million, an increase of 13.8 percent compared with 1Q02 and 48.7 percent compared with 2Q01. EBITDA(1) (earnings before interest, taxes, depreciation and amortization, excluding noncash deferred compensation expenses and goodwill impairment charge) loss margins also improved significantly to 6.4 percent, with a consolidated EBITDA loss of $11.8 million for 2Q02 before giving effect to an additional $9.3 million expense primarily relating to Allegiance's exposure to WorldCom and certain other financially troubled carriers. The Company also took a noncash charge of $110.8 million for the estimated impairment of goodwill pursuant to the requirements of Statement of Financial Accounting Standards (SFAS) 142.

(1) EBITDA means earnings before deducting interest, taxes, depreciation, amortization, non-cash deferred compensation expenses and goodwill impairment charge and is not derived pursuant to generally accepted accounting principles, and therefore should not be construed as an alternative to operating income (loss), as an alternative to cash flows from operating activities, or as a measure of liquidity.

"The second quarter marked a major inflection point in our continued path to profitability," said Royce J. Holland, chairman and CEO of Allegiance Telecom. "For the past 15 quarters while we were building out our 36 markets, Allegiance operated at a controlled cash burn rate with quarterly EBITDA

losses ranging from approximately $22 million to $32 million. Excluding the $9.3 million principally related to a provision to reserve potential exposure to WorldCom and other distressed carriers, Allegiance Telecom saw an EBITDA improvement of almost $10 million in the second quarter 2002 compared to the first quarter of 2002. We expect to see the same dramatic improvement in the third quarter and expect to turn EBITDA positive late in the quarter," he said. "I am also pleased that Allegiance accomplished this while achieving top line organic growth of approximately 11 percent over the first quarter, not counting the small contribution from the acquisition of the CPE and service businesses from WorldCom. A significant contributor to this dramatic improvement in revenue growth is a reduction in churn in our retail customer base," said Holland.

36-City Network

Allegiance Telecom's U.S. markets include: Atlanta, Austin, Baltimore, Boston, Chicago, Cleveland, Dallas, Denver, Detroit, Fort Lauderdale, Fort Worth, Houston, Long Island, Los Angeles, Miami, Minneapolis/St. Paul, New York, Northern New Jersey, Oakland, Ontario/Riverside CA, Orange County, Philadelphia, Phoenix, Pittsburgh, Portland, Sacramento, St. Louis, San Antonio, San Diego, San Francisco, San Jose, Seattle, Tampa, Washington D.C., West Palm Beach/Boca Raton and White Plains, NY.

Allegiance Telecom increased its addressable market during 2Q02, adding 14 new colocations. At the end of June, the Company was colocated in 829 central offices for unbundled loops, representing an addressable "on-switch" market of approximately 21.63 million local business access lines.

Allegiance has 31 telecommunications switches in operation, supporting the following markets: Atlanta, Austin, Baltimore, Boston, Chicago, Cleveland, Dallas & Fort Worth (2), Denver, Detroit, Houston, Los Angeles, Miami & Ft. Lauderdale & West Palm Beach/Boca Raton, Minneapolis/St. Paul, New York & Long Island & White Plains (2), Northern New Jersey, Orange County & Ontario/Riverside, Pittsburgh, Philadelphia, Phoenix, Portland, Sacramento, St. Louis, San Antonio, San Diego, San Francisco & Oakland, San Jose, Seattle, Tampa and Washington, D.C.

Financial and Operational Highlights

Allegiance Telecom's line sales remained strong with 210,000 lines sold in 2Q02, equal to the 210,000 lines sold in 1Q02 and an increase of 9.4 percent compared with 2Q01. Net lines installed during the quarter totaled 106,700, negatively impacted by the termination by Qwest Communications of service on approximately 58,000 managed modem port lines. Allegiance Telecom had anticipated this termination and has incorporated the termination of these lines into its outlook for the remainder of 2002. Average revenue per line increased to $51.54 in 2Q02, up from $50.16 in 1Q02 and from $50.08 in 4Q01.

As discussed in the first quarter 2002 results, reducing customer churn, especially in Allegiance's smaller unbundled loop customer base, is a top priority for the Company. Excluding the impact of the 58,000 Qwest wholesale lines, the overall churn rate was 2.4 percent, compared with a churn rate of

2.7 percent in 1Q02.

This improvement is primarily the result of four initiatives: (1) Implementation of electronic interfaces linking the order management, provisioning, and billing systems for unbundled loop customers to eliminate the manual entry of installation and disconnect data into multiple systems; (2) Implementation of electronic bonding with the ILECs for trouble ticket management in 16 markets; (3) Improvements in the billing dispute resolution and collection processes; and (4) A growing percentage of larger integrated access customers under longer term contracts and a continuing reduction of the number of resale customers.

"We implemented a number of process improvements and system automations late in the first quarter and during the second quarter to reduce churn," said Dan Yost, Allegiance's president and chief operating officer. "In 3Q02, we plan to continue the implementation of the Singl.eView by ADC billing system for new customers for most of our markets, with the implementation complete for all markets by November. Concurrent with this, Allegiance will activate an electronic interface linking Singl.eView with the rest of the systems for integrated access and other T-1 based customers. Even though we are encouraged with the progress made in reducing churn, we are not satisfied and expect continued improvement in the third quarter," said Yost.

"The number of net installs for integrated access and other T-1 delivered voice and data services continues to exceed the net installs for unbundled network element (UNE) loop services. This represents a significant positive trend; integrated access continues as Allegiance Telecom's fastest growing product, continuing to make rapid gains in terms of our base of lines," said Tony Parella, president, telecom and retail services, for Allegiance Telecom. Parella also noted that Allegiance has established electronic bonding for trouble tickets with the incumbent carrier in 16 markets, creating a smoother, more accurate workflow to resolve problems.

Before giving effect to the provision related primarily to WorldCom and other distressed carriers, EBITDA loss as a percent of revenue for the second quarter 2002 was 6.4 percent versus 13.4 percent in 1Q02 and 22.7 percent for 2Q01. Capital expenditures were $42.4 million in 2Q02, which is a 63 percent reduction compared to 2Q01.

"Allegiance Telecom significantly controlled its cash burn in the quarter, using approximately $82.3 million of its cash and short-term investments during the second quarter to fund its operations, capital expenditures and service its indebtedness," said Thomas M. Lord, Allegiance executive vice president of corporate development and chief financial officer. "For the first half of 2002, cash burn totaled $149.6 million, a reduction of 53 percent from the first half of 2001. We expect to see further significant improvement in the last half of 2002," he said.

"We have also drawn down our $150 million senior revolving credit facility, with $135 million funded to date. Three of our twenty-six senior lenders have not yet funded and we are engaged in discussions with them to respond to their requests for additional information. At June 30, 2002, after giving effect to this funding, Allegiance had approximately $354.0 million of

cash and short-term investments. This figure reflects the considerable decline in Allegiance Telecom's quarterly cash consumption," said Lord.

"We remain confident in our ability to remain in compliance with our senior credit facility for the remainder of this year and beyond," Lord continued. "In our view, the primary financial covenants are the requirement to achieve gross revenue of $200 million and $220 million in the third and fourth quarters of 2002, respectively, and the requirement to maintain a ratio of senior secured debt to annualized consolidated EBITDA (i.e., the EBITDA for any quarter multiplied by four) of 5.0 to 1.0 for the first quarter of 2003; 4.0 to 1.0 for the second quarter of 2003; and 3.0 to 1.0 for the third quarter of 2003 and all quarters thereafter. We believe we are on plan to achieve these levels of performance. Our senior lenders, however, have asked us to engage in discussions with a view towards modifying our senior credit facility to place a greater emphasis on profitability and cash preservation, with less emphasis on growth while also strengthening some of the restricted covenants in the facility. We have begun these discussions, but do not plan to entertain any request to reduce the size of our credit facility or otherwise materially limit the availability of funds under the facility."

Acquisition of WorldCom Customer Premise Equipment Businesses

In mid June, Allegiance Telecom, Inc. finalized its acquisition of WorldCom, Inc.'s customer premise equipment (CPE) provisioning business and its CPE maintenance business. The aggregate purchase price was $30 million in cash. Together, these businesses represent one of the largest providers of CPE maintenance service and one of the largest CPE distributors in the U.S., with more than 5,000 customers nationwide in more than 7,000 locations. The businesses operate in 34 major U.S. markets, 25 of which are also served by Allegiance.

The acquisition of these businesses accelerates Allegiance's emphasis on integrated service offerings to businesses using state-of-the-art CPE. It also strategically enhances Allegiance's growing national accounts business as nationwide or regional customers seek "One source for business telecom(TM)." With these transactions, Allegiance now offers a truly complete communications solution to corporate customers, including local and long distance voice, and Internet access services, now bolstered by a full suite of customer premise communications equipment and service offerings.

Early Markets Continue To Demonstrate Move Toward Profitability

To demonstrate its progress toward profitability, Allegiance Telecom began reporting operating results in 4Q00 for nine of its markets that began service in 1998 or early 1999 that became pre- overhead EBITDA positive during the fourth quarter (before corporate overhead allocation). These nine markets were Dallas, New York, Atlanta, Fort Worth, Chicago, Los Angeles, San Francisco, Boston and Houston. In the first quarter of 2001, Philadelphia and San Diego turned pre-overhead EBITDA positive, as did Baltimore and San Jose during the second quarter. During 3Q01, Orange County became pre-overhead EBITDA positive, while Northern New Jersey and Denver joined the club in 4Q01.

This year, Detroit and Phoenix, became pre-overhead EBITDA positive during 1Q02, and Washington, D.C. and Oakland reached this status in 2Q02 to bring Allegiance's total to 20 pre-overhead EBITDA positive markets.

More information on the performance of these markets is included in the financials attachment of this 2Q02 news release.

Regulatory Certifications

Allegiance Telecom is certificated to provide local exchange services in 24 states and Washington D.C., including Arizona, California, Colorado, Florida, Georgia, Illinois, Indiana, Minnesota, New Jersey, New York, Maryland, Massachusetts, Michigan, Missouri, Nevada, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, Texas, Virginia, Washington State and Wisconsin.

Corporate Background

Based in Dallas, Allegiance Telecom is a facilities-based integrated communications provider (ICP) offering businesses a complete package of telecommunications services, including local, long distance, international calling, high-speed data transmission and Internet services. Allegiance is currently operational in 36 U.S. markets. The Company's Web address is: www.algx.com. Allegiance's common stock is traded on the Nasdaq National Market under the symbol ALGX.

Certain statements in this press release constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, and the Company intends that such forward- looking statements be subject to the safe harbors created thereby. The words "believes," "expects," "estimates," "anticipates," "plans," "will be", "should" and "forecasts" and similar words or expressions identify forward-looking statements made by or on behalf of the Company. These forward-looking statements were derived using numerous assumptions and are subject to many uncertainties and factors that may cause the actual results of the Company to be materially different from those stated in such forward-looking statements. Examples of such uncertainties and factors include, but are not limited to, the Company's ability to timely and effectively provision new customers; the Company's ability to retain existing customers; the Company's ability to obtain additional financing should it be necessary to do so; the Company's ability to develop and maintain efficient billing, customer service and information systems; and technological, regulatory or other developments in the industry and general economy that might adversely affect the Company. Additional factors are set forth in the Company's SEC reports, including but not limited to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2002. The Company does not undertake any obligation to update or revise any forward-looking statement made by it or on its behalf, whether as a result of new information, future events or otherwise.

PRN Allegiance Telecom Announces Double Digit Sequential Revenue
Jul 30 2002 16:01

ALLEGIANCE TELECOM, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Dollars in thousands, except share and per share amounts)
Unaudited

	Three Months Ended June 30, 2002	Three Months Ended June 30, 2001	Six Months Ended June 30, 2002	Six Months Ended June 30, 2001
Revenues	$184,437	$124,059	$346,532	$229,933
Network Costs	95,323	60,801	177,401	112,029
Gross Margin %	48.3%	51.0%	48.8%	51.3%
Selling, General and Administrative	110,249	91,394	212,033	176,016
Depreciation, Amortization and Noncash Compensation	71,581	61,985	140,051	119,402
Goodwill Impairment Charge	110,823	-	110,823	-
Loss From Operations	(203,539)	(90,121)	(293,776)	(177,514)
Other Income (Expense)				
Interest Income	2,066	3,181	3,811	10,229
Interest Expense	(25,342)	(16,398)	(49,440)	(32,393)
Other Income (Expense), net	(23,276)	(13,217)	(45,629)	(22,164)
Net Loss Applicable to Common Stock	$(226,815)	$(103,338)	$(339,405)	$(199,678)
Net Loss Per Share, basic and diluted	$(1.94)	$(0.92)	$(2.90)	$(1.79)
Weighted Average Shares Outstanding, basic and diluted	117,016,288	112,856,763	116,895,377	111,799,824
Other Financial Data:				
EBITDA (1)	$(21,135)	$(28,136)	$(42,902)	$(58,112)
EBITDA before charges related primarily to WorldCom exposure (2)	(11,801)		(33,568)	
Capital Expenditures	42,429	114,777	82,251	230,605

Notes:
(1) EBITDA excludes noncash compensation expense and goodwill impairment charge.
(2) Excludes certain charges incurred during 2nd quarter 2002, including provisions for exposure to WorldCom and certain other carriers

ALLEGIANCE TELECOM, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except share amounts)

	June 30, 2002 (unaudited)	Dec. 31, 2001
ASSETS		
CURRENT ASSETS:		
Cash, cash equivalents, and short-term investments	$354,042	$399,316
Other current assets	219,132	167,090
Total current assets	573,174	566,406
PROPERTY AND EQUIPMENT		
Property and equipment	1,474,345	1,366,710
Accumulated depreciation	(464,375)	(350,460)
Total property and equipment, net	1,009,970	1,016,250
NON-CURRENT ASSETS (1)(2)	70,822	192,187
TOTAL ASSETS	$1,653,966	$1,774,843
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES	$178,760	$139,474
LONG-TERM DEBT	1,188,734	1,013,184
OTHER LONG-TERM LIABILITIES	13,681	14,109
STOCKHOLDERS' EQUITY	272,791	608,076
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$1,653,966	$1,774,843
COMMON SHARES OUTSTANDING	122,762,131	115,214,859

Notes:

(1) Includes restricted long-term investments of $934 and $954 at June 30, 2002 and December 31, 2001, respectively.
(2) Non-current assets at June 30, 2002 reflect a goodwill impairment charge in accordance with SFAS 142

Selected Operational Statistics

	As of June 30, 2002	As of March 31, 2002	As of December 31, 2001	As of June 30, 2001
Markets Served	New York	New York	New York	New York
	Dallas	Dallas	Dallas	Dallas
	Atlanta	Atlanta	Atlanta	Atlanta
	Fort Worth	Fort Worth	Fort Worth	Fort Worth
	Los Angeles	Los Angeles	Los Angeles	Los Angeles
	Chicago	Chicago	Chicago	Chicago
	Boston	Boston	Boston	Boston
	Oakland	Oakland	Oakland	Oakland
	San Francisco	San Francisco	San Francisco	San Francisco
	Philadelphia	Philadelphia	Philadelphia	Philadelphia
	Washington, D.C.	Washington, D.C.	Washington, D.C.	Washington, D.C.
	San Jose	San Jose	San Jose	San Jose
	Orange County	Orange County	Orange County	Orange County
	Houston	Houston	Houston	Houston
	No. New Jersey	No. New Jersey	No. New Jersey	No. New Jersey
	Long Island	Long Island	Long Island	Long Island
	San Diego	San Diego	San Diego	San Diego
	Detroit	Detroit	Detroit	Detroit
	Baltimore	Baltimore	Baltimore	Baltimore
	Denver	Denver	Denver	Denver
	St. Louis	St. Louis	St. Louis	St. Louis
	Cleveland	Cleveland	Cleveland	Cleveland
	Seattle	Seattle	Seattle	Seattle
	Miami	Miami	Miami	Miami
	Minneapolis/ St. Paul	Minneapolis/ St. Paul	Minneapolis/ St. Paul	Minneapolis/ St. Paul
	Phoenix	Phoenix	Phoenix	Phoenix
	Tampa	Tampa	Tampa	Tampa
	San Antonio	San Antonio	San Antonio	San Antonio
	Ft. Lauderdale	Ft. Lauderdale	Ft. Lauderdale	Ft. Lauderdale
	Austin	Austin	Austin	Austin
	Sacramento	Sacramento	Sacramento	Sacramento
	Portland	Portland	Portland	Portland
	White Plains	White Plains	White Plains	